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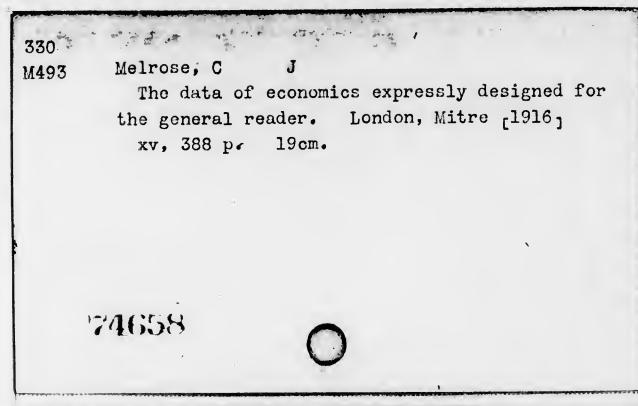
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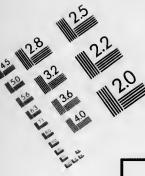
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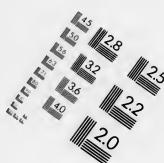
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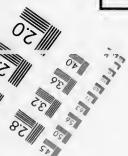
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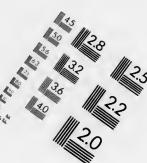
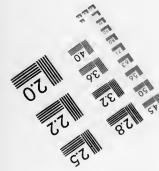
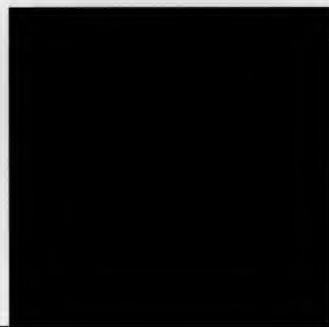
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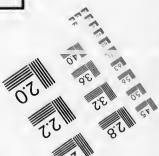
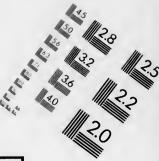
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THE DATA OF ECONOMICS

THE
DATA OF ECONOMICS

EXPRESSLY DESIGNED FOR
THE GENERAL READER

BY
C. J. MELROSE



LONDON
THE MITRE PRESS
1, MITRE COURT, FLEET STREET, E.C.

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TO
MY GOOD FRIEND
THOMAS J. JAMES, Esq.

This Book
IS GRATEFULLY DEDICATED

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PUBLISHERS' NOTE

THIS book was ready to be published in September, 1914 ; but when the war broke out it was thought desirable to postpone publication. At the urgent pressure of many subscribers, however, we have decided to bring it out now, and put up with the necessarily adverse effect on circulation.

The author thought it desirable to partly rewrite Chapter XV. For the rest, it remains as it was prepared for publication in 1914. It says much to the credit of the book that there is practically nothing in it that needs correction, or has gone out of date.

PREFACE

THE purpose and justification of this treatise may be summed up in these three sentences :

1. An attempt to translate the economic process from terms of "money" into terms of "things and services"—comprehensively, "utilities."
2. To present a connected outline of the essentials—the framework—of the economic mechanism of production in a way that will appeal to the general reader.
3. To marshal the points in a manner analogous to the inductive as opposed to the deductive method—*i.e.*, instead of starting from the complex generalisations of the modern industrial machine and analysing them into their constituent parts, the endeavour is to build up from the simple to the complex.

To the "man in the street" the Mercantile Theory still remains the sole economic conception ; and this notwithstanding that he may have learned to repeat the formula that "money is the medium of exchange." The economic student has professedly discarded that preposterous crudity ; but in the vast majority of cases the intellectual assent has

wholly failed to eradicate the crystallised conception. Where the impression has been really modified in some degree, it frequently carries the student little beyond the mere elements. As soon as he gets into the more complex aspects, the terms employed carry him irresistibly and unconsciously back into the old conception. Even many writers on economics have not escaped the demoralising influence of the terminology of the market. The economist is yet to come who will do the world the inestimable service of stating the problem in terms of the reality—products and services—instead of in terms of that which, even when tangible, is only a contrivance to facilitate exchanges; and which, under modern conditions, has largely ceased to be tangible at all, being no more than an ideal contrivance—a purely psychological factor. Within the limits and scope of this treatise, the attempt is here made in this direction. The term "money," or some other word-symbol standing for that idea, cannot be entirely eliminated from an economic investigation. But in every case where I thought a misconception probable or possible when dealing with the issues usually conceived in terms of money—*e.g.*, income, rent, profit, interest, wages, and so on—the terms are so explained and qualified as to avoid any reversion to the false conception of the process for which the use of the term and that which it commonly conveys is mainly responsible. I was trying recently to make someone understand that real wealth consists of things capable of satisfying human desires—as land, houses, food, clothing, furniture, works of art, books,

and so forth. "Oh yes," he replied promptly, "I understand—anything that can be turned into money." In the course of our investigation I shall, I am confident, have no sort of difficulty in showing that, while the man of average education would not put it quite so crudely as this, it is, nevertheless, the prevailing conception behind all the verbal masquerade. The cat of nine lives, or of ninety million lives, is the merest ephemeral beside the imperishable Mercantile Theory of Economics.

The general reader I have in mind is that reader who, by the fact that he desires to read a book on economics, may be trusted to follow a chain of reasoning when stated lucidly and convincingly, though not escaping the complexity inevitable to the subject. He is not assumed to have any previous knowledge of economics; and no attempt is made to carry his assent by sheer weight of authority, but only by an appeal to his reasoning faculty. I have purposely abstained from any reference whatever to the views of authoritative writers, preferring to leave the arguments to stand on their merits. The reader is invited to hold his critical faculty keenly on the alert against any inconclusive reasoning. Should I have succeeded in whetting his appetite for a further study of the subject, it is hoped that this treatise may prove a useful preparation; but in all cases he is warned to accept no proposition which falls short of carrying the fullest reasoned conviction.

The professional critic may take it as a general statement that I lay no claim to any originality whatever,

PREFACE

beyond the purpose stated at the outset. It is a matter of a change of dialect and newly arranged sequence, rather than a change of first principles. In the matter of dialect I have only one aim in view—to use only such terms and expressions as will most clearly convey the conceptions for which they stand as symbols, regardless of the terminology of the classic writers on this subject. Should I have succeeded in presenting the case as lucidly and convincingly as my vanity leads me to believe—a vanity which is established by the fact of authorship, spite of conventional protestations of humility—it may haply be that this treatise will not be without use to the student also. That there is ample room for an exposition on these lines is, I think, entirely beyond question.

C. J. M.

AUTHOR'S NOTE

OWING to its somewhat abstract and psychological character, what is now the Preliminary Chapter was intended to appear as an Appendix. But on second thoughts, its importance to the student and critical reader was held to outweigh the objection that its appearance as an opening chapter scarcely bears out the professed intention of presenting the problem "in a way that will appeal to the general reader." The reader who does not care to bother his brains with disputations on definitions may begin from Chapter I., in full confidence that the contents of the Preliminary Chapter do not in the least affect any of the subsequent reasoning—that is, provided he is not disposed to question any of the definitions given. Should he already be impregnated with the widely prevalent "definition bacillus," he must fly to the only remedy—a careful reading of the chapter "On Definitions."

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THE DATA OF ECONOMICS

PRELIMINARY CHAPTER*

ON DEFINITIONS—AND ON TERMINOLOGY GENERALLY

THE reader who has dived into the study of science to however modest an extent—and who has not nowadays?—becomes impressed early in his studies with the importance attaching to accurate definition. Unfortunately, the idea which he forms of the purport and importance of correct definition frequently contains a misconception so radical as to constitute a stumbling-block rather than a help. Most of us are familiar with the shallow thinker whose sole resource by way of criticism consists in fastening upon what he holds to be a wrong definition: maintaining that, since the definition given is wrong—*e.g.*, that “wealth” or “capital” really means something more or something less than had been defined—the whole reasoning is vitiated at the source, and may be dismissed as utterly worthless. Then, there are those who would build up the science of economics—after the fashion of a certain school of metaphysics—on a series of cast-iron definitions, superimposed one on the other—a sort of “House that Jack built”—for all the world as if all that needs be done is to make up the moulds, into which the facts and events in nature will have to fit themselves, willy-nilly. Seas of

* See Author's Note.

ink have been spilt in wrangling about definitions ; the average teacher of economics thinks it necessary to drill his class at the outset into an acceptance of a long string of definitions ; and in the end we are little further advanced than we were before.

Put concisely—not to say epigrammatically—the ordinary idea of a definition is that it defines a “thing” ; whereas all that it does is to define a “conception.”

Now, to make this quite clear. The world is full of untold millions of individual objects, no two of which are exactly alike. What is it that you mean when you say that they differ ? You mean that each presents certain distinctive qualities to our senses. Some of the objects differ widely, while others, though not quite alike, bear a more or less close resemblance ; but each presents to our perception something distinctive—whether it be in size, shape, colour, taste, smell, consistency, and so on. An apple differs very much from an elephant, or a church steeple ; but it also differs from a pear ; one variety of apple, a Ribston Pippin, differs from another variety, a Blenheim Orange ; nay, even in the same variety no two apples are quite alike.

Now, a particular kind of apple does not take on its qualities of taste, colour, shape, and so forth because you choose to call it a Ribston Pippin ! On the contrary, you give it that name by way of sign or symbol, so that the word may recall to your mind the conception of a set of qualities which you are accustomed to associate with a certain object. First, then, comes the mental classification, based on conceptions of difference in qualities or attributes, and then come the verbal symbols by means of which the conceptions are visualised. The ability to differentiate

and classify does not come all at once, but is a matter of gradual mental evolution.

Taking them in what are probably the reverse of the order of conception, you invent word-symbols which will recall to your mind the distinctive characteristics of the varieties—you call a certain apple a “Russet” so that the name may present to your mind just those qualities in which it differs from a Blenheim Orange, a Ribston Pippin, and dozens of other varieties. Then comes the general name of the species “apple” which recalls to mind, not the particular qualities in which the varieties differ one from the other, but, on the contrary, the conception of likeness—those more widely diffused qualities common to the species, the qualities in which the varieties are alike or very similar—*e.g.*, taste and shape. Further comes the generic name of “fruit,” a conception of qualities still more widely diffused, possessed in common by objects so widely dissimilar as the apple, pear, plum, cherry, apricot, and dozens of other species. And finally we have the scientific conception of the vegetable kingdom, standing for a likeness based on qualities still more widely diffused, applied to all objects rooted in the soil, growing by means of internal assimilation, which reproduce their species.

Let us now see where we stand. Two apples of the same variety—*e.g.*, the Russet—are unlike in size and shape, but are practically alike in every other respect. The size and shape, then, are qualities particular to each—we should call that “individual variation”—but as regard taste, colouring, texture of skin, etc., the qualities are general to the whole of that variety. If, then, we compare a Russet with another variety—*e.g.*, the Blenheim Orange—we see that they are unlike also in colouring, texture of skin, consistency, and to some extent in taste also, while yet alike in many other respects. Thus, the qualities

which were general as between the members of the Russet variety, now become particular as between the Russet and the Blenheim Orange, while yet possessing other qualities general to both. But when the apple is compared with another species classed together under the name of "fruit"—*e.g.*, the pear, plum, or orange—the difference in colour, taste, texture of skin, consistency, and so on, is very much accentuated, and there are also pronounced differences in structure and other details, while yet they possess many and striking qualities in common. Thus, the qualities which were general as between the Russet and the Blenheim Orange now become particular as between the species apple and the species plum; whilst there are other still more diffused qualities general to all the species of the genera "fruit," in edibility, saline properties, and so on. Put in another way, in so far as they differ, one is an apple and the other is a plum; but in so far as they are alike, both are fruit. If, then, we compare fruit with certain edible vegetables, the differences are still more striking, while yet they possess certain general qualities in common. And when finally we make the comparison between these and plant life as a whole, many of the qualities which are general between fruit and edible vegetation now become particular to them as compared with the beech or oak; while yet they have certain very important qualities in common which entitle us to class them together as members of the "vegetable kingdom," inasmuch as they all feed, grow, and reproduce—qualities which we conceive to constitute "life"—as being living organisms.

Now, will anyone in his right senses maintain for a moment that he can draw a clear-cut line of demarcation marking off the particular qualities of the Blenheim Orange from those other more general qualities with which entitle us to class it with other varieties as an

"apple"? Can he tell me the exact line of cleavage between the qualities which make us class both as apple and the more widely diffused qualities conceived under the generic name "fruit"? Where does the one leave off and the other begin? Is there, indeed, any such line of demarcation? Are not these qualities merging into each other and overlapping at many points? What, indeed, are the actual qualities which give the general idea of fruit? Should rhubarb and tomatoes be classed among fruit or vegetables? Our classification is sound enough in so far as it relates to clearly marked likenesses and differences, but it breaks down the moment it is conceived as marking off distinct lines of cleavage in nature. In the region of abstract conceptions we are, if anything, still more helpless.

What, then, is a definition? One means by a definition something more than a mere description. In the strict sense, a definition is demanded when a term is employed in a reasoning process, for the purpose of drawing some logical deductions from the related ideas under consideration. To define, then, is to limit, circumscribe, to put within definite boundaries, to establish clean-cut lines of demarcation—in short, to do the very thing which, if applied to objects, facts, and events in nature, it is utterly impossible to do.

Nature is not made up, as some people apparently imagine, of definite layers of phenomena, superimposed one on the other. There is no definite line of cleavage anywhere in nature. The whole zoological tree, all varieties, species, classes, and genera merge imperceptibly one into the other. The animal kingdom merges into the vegetable and the vegetable into the mineral. The facts of sociology, the events in the lives of men and their social relations to each other, are no exception to the rule—

unless one were to say that they are "only more so." Here, as elsewhere, while some of the differing attributes stand out distinctly enough, others are constantly overlapping and imperceptibly merging one into the other. Fix your line of demarcation where you will, you will presently come on something which is sprawling right across your line, making your classification apparently a mere house of cards.

Does it, therefore, follow that definition is both unnecessary and useless? By no means. We only have to remember that what we are limiting, circumscribing, and putting within rigidly defined boundaries are not the objects or events in nature, but our own conceptions—the conceptions of the particular attributes which are made the subject of our investigation. If our conclusion is to be valid, the definition must be true to facts—by which is meant that the attributes predicated must be actually manifested by the object, fact, or event under review; but it matters not in the least if on either side of these attributes there are others not touched by the definition; or if, under other conditions, the attributes predicated gradually shade off into others, or are overlapped by others. What does matter is, that we shall reason correctly from our premises. The "term" is the symbol which stands for and recalls the conception, but not the "thing." As is not unfrequently the case, this truth can best be expressed in the form of a paradox. It is this very fact of the absence of definite lines of cleavage in nature that makes the need of accurate definition in scientific reasoning so very imperative. The facts will not break bounds—they are always what they are—but your conceptions almost certainly will without you restrain them most rigidly. Unless you cut one thought quite clear from another, they will almost certainly shade off on

either side into all the colours of the spectrum. You must keep your thoughts confined to "one thing at a time" if you want to reason correctly.

Controversies about definitions assume that the limitation of the conception must have a corresponding limitation in external facts. But this is not so. A classification is none the less valid, though the attributes on which it is based does not exhaust all the attributes contained within the objects or events classified, or because of the final merging and overlapping in nature. Nor is a logical conclusion necessarily unsound because all the attributes are not taken into account. It is only necessary to postulate the quality of hardness in iron to conclude that if thrown with sufficient force it will break glass; you are not bound to know the other qualities of the metal. All that matters is that the conclusion should follow exactly from your premises.

An example from the subject which we are about to investigate will, perhaps, make the point stand out more clearly. The term "wealth" has a commonly accepted significance which requires little by way of definition. But some writers on economics will have it that acquired skill and knowledge should be included in the meaning of the term wealth. Now, it is obvious that the man who is skilled in some trade or profession is better equipped than the man who is not; and it is equally obvious that, under present conditions, skill is not as readily exchangeable for bread and butter as is money or marketable commodities. Except only that the latter meaning apparently needlessly alters the commonly accepted significance, it matters nothing to correct reasoning what definition you adopt. If it is agreed that the term shall be used in the wider sense, some other term will have to be found for signifying the narrower conception. Whatever the terms used, you

do not alter the facts—the man of skill will have the advantage whether you say that he has wealth, or potential wealth, or any other name you like to give it.

Take the simple proposition which everyone would readily grant: A—B has wealth, and therefore cannot be in want. But see what becomes of your proposition if you widen the conception of wealth to include skill. A—B (being a skilful bricklayer) has wealth, and therefore cannot be in want—a conclusion which we know unfortunately to be frequently untrue. And yet it may well be true under other conditions—if the demand for bricklayers were greatly to exceed the supply. The proposition implies a major premise which it omits to state explicitly. Take the condition of the bricklayer as just assumed. The syllogism stated in full would then be true of the bricklayer, thus: Wealth consists in the possession of things which satisfy desires or of qualities which command those things: A—B has wealth (in possessing a quality which commands things); therefore A—B cannot be in want (of those things). It scarcely, however, requires the aid of the syllogistic form to make the point quite obvious.

A definition should isolate and put within boundary lines just that conception which is essential to the elucidation of the subject in hand. A preconceived notion of how a term should be defined, either on grounds of etymology or on any other *à priori* grounds, is about the most gratuitous folly imaginable. The upshot of our analysis is simply this: that there is no such thing as a wrong definition. So far as the reasoning process is concerned, it follows just as cogently and correctly from hypothetical premises; but, of course, if the hypothesis should prove not true in nature, the conclusion falls with it—this much is perfectly understood in all deductive reasoning. One may reasonably object to the use of a term contrary to its generally accepted

and well-established meaning among students of the particular science, on the ground that it will lead to needless confusion. But that is quite a different matter from asserting that a definition is wrong unless corresponding lines of demarcation are found in nature. So long as the conclusion follows from a conception true to nature within the limits defined we shall not be far wrong.

Those who know something of what has been written on economics will, I feel sure, not think that the point has been laboured needlessly. It is well worth some effort to get rid of the endless and perfectly futile wrangles about definitions. Other sciences are almost entirely free from this futility. It is time for economics to shake off this incubus.

There is, however, this to be remarked that, unlike other sciences which have practically wholly technical terminologies, the science of economics is not a little handicapped by the employment of a great number of terms which are in common daily use. Now, it is in the nature of such common usage that, not only do the terms fail in precision of thought, but they are largely used in a figurative sense, and barely convey an identical significance to any half-dozen persons taken at random. As we proceed with our subject we shall become fully conscious of this drawback. However, what cannot be cured must be endured. Since the coining of a wholly new terminology is out of the question, it becomes all the more incumbent upon us to so clearly limit the thought as to leave no room for straying from the significance agreed to be assigned to the respective terms used.

CHAPTER I

INTRODUCTORY REMARKS

ECONOMIC science sets out to investigate the laws governing the production of wealth under varying conditions, with a view to discovering the methods most conducive to increased production. In a strictly direct sense the ethical issue of a more equitable apportionment of wealth between the social units is outside the scope of economic study. As an individual, the student may, perhaps, be allowed here and there to give expression to his personal views; but *qua* economist, his work is to discover the mechanism which tends to a maximum of productive efficiency, leaving to religion and ethics the duty of advocating a more equitable distribution of the increased wealth. The ethical condition of the social fabric is, of course, in itself a factor of great potency in the adjustment of the mechanism. It is not an economic machine plus a congeries of human beings, but it is the human beings which make up the machine; hence the mental and moral condition of the humans cannot fail to be factors in the working of the mechanism. Whenever, therefore, the ethical teachers and preachers succeed in creating a fresh moral outlook, the economic machine will have been modified to that extent. Of that the student of economics is bound to take cognisance, but he can do little himself

towards creating that new outlook. It requires the genius of a Ruskin to combine the two with any degree of success.

Nevertheless, in a way barely deflected from the direct, the science of economics is in very essence a magnificent sermon on social equity. While wealth is conceived as consisting in the acquisition of gold, it follows that there are only two alternatives. If all of mankind were fortunate enough to have gold mines in their back gardens, then we could all be wealthy together; but since Providence has denied us this inestimable boon, then there is nothing left for it but to scramble for the biggest share of what gold there is, since the more someone else gets the less there is for you. But no sooner is it realised—I say *realised*, not merely granted or assented to—that wealth consists in the utilities for the satisfaction of human needs and desires created by human hands and brains, than the whole economic conception assumes a new and entirely different aspect. Wealth, then, ceases to be a fixed quantity to be scrambled for, catch-as-catch-can. There may be a limit to human capacity for producing wealth; nature will not yield all that man could desire, nor will it yield anything at all without human labour; but that limit is not yet—not by a very long way. That wealth which it actually does yield may or may not be equitably apportioned as a just reward of productive efficiency—this is a question for the teachers of religion and ethics. But over and above that question of equitable share looms the vital question, Are we extracting from nature as much wealth as she is capable of yielding? Is our economic mechanism adjusted for the attainment of the best possible results? Is it practicable to so adjust the economic machine that, while the share of utilities which are the reward of higher ability or efficiency—or even of mere privilege of birth—may be no smaller than it is now, that share which now

falls to the poor and less efficient may be made much bigger? Can, in short, the economic machine be made more productive of wealth than it is at present? These are the questions for the economist. Without he can give an answer to these questions—unless he can answer them in the affirmative—then is economics, indeed, an idle speculation, leading to no practical results.

But in the answer to these questions is involved the ethical issue which, *per se*, is not directly within the province of economics. Since it is the human units which are the cogs in the economic machine, the mental and moral conditions are factors of enormous magnitude in the efficient working of the mechanism. Experience has demonstrated beyond shadow of doubt that a condition of slavery is enormously less efficient as a producing machine than a condition of freedom. The conviction is being forced upon us daily that the worker who lives in a state of degradation and economic hopelessness is less efficient as a producer than the worker who lives in comparative comfort, with an inspiration of hope for the future. You may drive a man to work on your own terms, but, not only can you not make him give of his best, but the very act of driving automatically brings his best down to the level of another man's worst. The driving power of the inanimate machine comes solely from without; but in the human machine the driving power from without must be supplemented by the driving power from within if the best results are to be attained. It may be that you make the reward commensurate with the result, so that, personally, you are no worse off; but in the meantime wealth which might have been produced is lost to the world, and it may well be that, had the reward been greater, both would have been better off.

Every engineer and mechanic knows that a machine

cannot be relied upon to work with any degree of smoothness unless all the parts are accurately fitted and carefully adjusted. But very few indeed can be made to see that the working of the economic machine is subject to exactly the same conditions. To them every piece of work stands alone and independent of the rest—a mere profit-making or wage-earning contrivance—just a means of transferring money from the pocket of one to the pocket of another. When we have learned to understand the complete inter-dependence of industries and the intimate linking-up of all the processes of production, we shall be better able to appreciate how much wealth is lost to the world through the ill-fitting and lack of adjustment of the parts of the economic machine. The maximum increase in the production of wealth is only to be attained by effective co-ordination of, and co-operation between, all the producing units ; by eliminating unproductive and wasted effort ; by each contributing his quota to the store of social service ; by not frittering away a part of a nation's energy in wars and preparations for wars ; by increasing the productive efficiency of each unit by means of education, physical and technical training, higher ethical conceptions of social aims and duties ; and last but not least, by conditions of life for every unit which develop reliance, self-respect, thought for the future and for the future of one's children. A nation does not escape the consequence of economic maladjustment by ignoring it. The prosperity of the few is by no means an index to a nation's progress. If the maladjustment is not sufficiently bad to cause decadence or complete stagnation, progress is arrested, at any rate, just at that point where the economic machine falls short of functioning at its best—and the best can only be attained by the smooth running of every part. This much economics cannot fail to teach, whether it wants to or not.

But there is yet another aspect to the question. As events are shaping the world over, it may well be that, in much more than a Spencerian sense, altruism will prove the best possible egoism. None but the mentally blind can fail to see that vast and rapid changes are taking place everywhere in the tissues of the social organism. The "have-nots" are clamouring for a larger share of the wealth which they help to create, and will not long be gainsaid. Political power is shifting to the side of the masses. The whole mechanism of industry, as we shall see later, has been undergoing a radical transformation, and is inevitably travelling to a certain definite goal. In place, therefore, of a violent scramble, under a rankling feeling of injustice endured, it may well be that a readjustment on ethical lines will prove the best possible "business investment." Be this as it may, the work of the economist is merely to elucidate the mechanism of wealth production and exchange, pointing the way to greater efficiency and consequent increase of wealth.

are improved and made more fit for human sustenance. Thus, while some remain hunters, others become nomadic shepherds, while the occupation of agriculture, mostly left to the women, is slowly being developed.

But human skill varies, and there presently comes someone who proves himself particularly skilful in the art of chipping rough flints into axes and spear-heads. By means of these he is able to capture more prey than his fellows, and so becomes the envy and admiration of his tribe. One unlucky day he gets lamed, and is unable to go hunting; and then someone is struck with the original idea that the flint-chipper might be induced to part with one or two of his spear-heads in exchange for meat. The exchange having been effected, the new owner now struts proudly along exhibiting his coveted possessions. But once an idea is discovered, others are not slow to take advantage of it. The flint-chipper—let us call him spear-maker—is tempted with all sorts of choice morsels; some are ready to build his hut, while others offer him skins or ornaments. Finding that sort of thing just to his liking, the spear-maker devotes more and more of his time to his favourite occupation; his reputation grows and spreads amongst neighbouring tribes, and so at last he becomes a professed spear-maker. The dunces in the art of flint-chipping find that it answers their purpose to give something that they possess in exchange rather than laboriously shape clumsy and ineffective weapons for themselves. And thus the occupation of weapon-maker becomes specialised. In course of time other trades and occupations become specialised in the same way. Barter between people and tribes has set in. "You make this, and I make that, and we'll exchange." Man begins to be dependent upon his fellows for the satisfaction of his needs.

With the differentiation of occupations and the intro-

CHAPTER II

BARTER—TRADES BECOME SPECIALISED—CO-OPERATION —EXCHANGE VALUE

PRIMITIVE man begins his human career as his own universal provider. He captures, gathers, or digs up his own food, selects his cave or other rough shelter, makes his own body-covering when driven to it by need, and fashions with his own hands what clumsy tools, weapons, and utensils he is capable of producing. In the struggle for survival, his wits become sharpened and his hands more skilful. Step by step, by degrees infinitely slow and painful, he invents means to protect himself against nature's inclemencies, to utilise the gifts which she is always ready to yield to human effort, to harness her forces to his services. In time he learns to domesticate certain species of animals. The genius arises whose benefaction to the human race stands out above all else—without which, indeed, no race that can truly be called "man" could have evolved. Man discovers the art of making fire artificially, by means of friction. The accidental burning up of a patch manures the ground, and the next crop of seed-grass yields a cereal richer and more robust. After many repetitions, the relation of cause to effect at last dawns on man's conception. Gradually he learns the art of cultivating the soil; cereals and other vegetable products

duction of barter begins the economic problem. Unaided by tools, and without the co-operation of his fellows, man can only live from hand to mouth ; each day has to provide for its own needs ; there is no period of sowing followed by a period of reaping ; there is no sense of prevision, no thought for the morrow. Of wealth, in any sense worth the name, there is none. As man advances in the art of making efficient tools and implements, means are opened up for getting from nature many things for the satisfaction of human desires which could not otherwise have been got at all ; while many other things, which were obtainable only in minute quantities at the cost of exhausting labour, are now produced in abundance. By devoting his energies principally to one occupation, the eye becomes more true, the hand more skilful, and the mind more capable of concentration. The desire to secure for his use the results of the labour of others, which he can only obtain in exchange for the results of his own labour, spurs him on to industry. Labour-saving devices, minute in themselves taken singly, but large in the total result, and pregnant with infinite consequences for the future, are thought out day by day. Man gradually develops the habit of steady application, his capacity as producer is constantly increasing, wealth is being created and accumulated. So far, there is little of interdependence between trades, and less of subdivision in the production of parts which are to constitute a single commodity. As yet money has not been invented, or even thought of.

It will be of inestimable advantage to a clear comprehension of our subject to reason out carefully so much of the economic issues as are applicable to such a simple state of society, before the complexity of modern production and the exchange medium have stepped in to cover up

and obliterate the connecting links. Before proceeding with our investigation, let us agree upon the conceptions to be represented by certain terms which it will be necessary for us to employ immediately. By "consuming" a thing we will mean usage in any form, whether it be food to eat, clothes to wear, a hut to live in, or pretty objects to look at. All things used get consumed in course of time—*i.e.*, they cease to exist in the form requisite for the satisfaction of human desires. The food may last only a few minutes, the clothes some months, the hut some years, the ornaments some centuries ; but in the end they all get consumed. Understood in this sense, the term stands for just that conception of wide significance which is material to the economic issue—there is nothing to be gained by a classification of "consumption" on the basis of durability. By a "commodity" we will mean an article consumed for its own sake, something that is used in the direct satisfaction of a desire. A "tool" is an article that is consumed, not for its own sake, but as a means to the end of producing something else which is to satisfy a desire. In a wider sense, the tool is classed together with implements, buildings, roads, and many other things, used for the purpose of production of wealth, under the generic name of "capital" ; but this is a matter which we shall reach in due course. These few definitions will be sufficient for our immediate purpose.

With an industrial mechanism and conditions of so simple a character in our mind's eye, we are in the best possible position to reason out the important question of "value," and much that follows from it : a question which is at the very basis of the economic problem. The issue before us is, What is it that governs the ratio at which things will exchange for each other ? In communities such as we have in view, hunting remains an important occupa-

tion long after pastoral and agricultural industries have developed to a considerable extent; practically every adult being tolerably proficient as a hunter. In the example we had before us of the demand for spears, we have as good a starting-point as any that could be chosen from which to follow up the laws governing exchange value.

Now, in the first place, almost everyone has some rough notion of what is known as the law of supply and demand. If many are clamouring for spears while the spear-makers are few, the hunters will be bidding against each other for the possession of spears, and their value will rise. On the other hand, if the spear-makers are many, each clamouring for customers, they will be bidding against each other to become possessors of, say, hunters' product, so that the hunters' product will rise in relation to spears; in other words, the value of the spears will fall. But is there no limit to the rise in value on the one hand, and the fall in value on the other hand? and if Yes, what governs the limit? There is no cost of production in the money sense that we understand it to-day; the spear-maker gathers his own flints, and cuts the saplings as needed—it is a question of less or more personal labour.

In the first place, then, what is the maximum quantity that the hunter will be willing to give in exchange for the spear? The answer to this ought to be fairly obvious. Since the spear is not an object desired for its own sake, but only as a means to the end of increased production of commodities—to enable the hunter to capture more prey with the aid of the professionally-made spear than he could have done with his club or jagged flint—the maximum that he will be willing to give for the spear will be something less than the increase in the capture which the spear enables him to effect. To follow the point more clearly,

we will speak of the product of the hunt as consisting of so many ideal units, be the unit one ounce, one pound, or one stone. If, then, we assume that he can capture ten units in a day without the spear, but can capture twenty units with it; if, for convenience of handling the figures, we assume further that the addition of two units to his income is the minimum inducement, he will be willing to give for the spear up to eight units. If as much as ten units is demanded, he ceases to have any interest in possessing the spear, since he can do as well hunting without it.

Incidentally, we may briefly interpolate here one or two useful lessons. Since the spear has value only as a means to the end of increased production, the spear-maker is in a true sense co-operating in the production, to the extent of the increase due to the use of his spear. We will call that the spear-maker's "productive efficiency." Further, it follows from this that the owner or contributor of any contrivance whatsoever, be it nothing at all tangible but merely mental, which brings about an increase in production, co-operates in the production, and is, therefore, a producer in the only sense that matters. Thus, the ability to organise a battue, or the mere supervision of the details, even if it consists of nothing more than giving orders, is a work of production, just in so far as the service is a necessary factor to the efficient accomplishment of the desired result. It comes to this, therefore, that a producer is anyone who renders a useful service—useful, that is, in the sense of being efficient. One man guides the plough, another follows with a basket and scatters seed in the furrow, while a third merely walks to and from the field and barn, refilling the baskets as they are emptied. Which of these is the producer? In fact, it is only nature that does the producing. All that man can do is to apply

to nature and fashion her gifts into forms useful to the satisfaction of human needs and desires.

Understood in this sense, what we know as "distribution" is really "production" in the economic sense. The term "distribution" is, indeed, used indiscriminately to denote two quite distinct conceptions. It is used firstly, perhaps mainly, to stand for the work of distributing the finished products amongst the various consumers. This includes all shopkeeping, whether wholesale or retail, the work of the merchant, speculator, and advertiser, and the transport of goods—in short, anything that has to do directly or indirectly with the handling and carrying of goods, as distinct from the actual working up of nature's materials into consumable utilities. But the term is also used to denote the sharing out, or apportionment, of the total product amongst the various social units. Thus, poverty is said to be the result of a bad "distribution" of wealth—that the few have too much, while the many have too little. The use of the term in this sense is manifestly quite a different conception. To denote this conception we shall use the term "apportionment." For the mere purpose of classifying employments, it is useful to differentiate the work connected with distributing the products amongst consumers from the work of shaping the materials, and from professional services generally. But for the wider economic conception of the production of utilities for the satisfaction of human desires, there is nothing to be gained by such a classification. All production is "service," whether material or immaterial, tangible or intangible; and no commodity can be said to be finished—*i.e.*, available for consumption—until it is in the actual possession of the consumer. Hence all those who contribute, directly or indirectly, to bring the commodity to the hands of the consumer are "producers" in the

economic sense. The student will find such a wide conception of production exceedingly helpful.

The maximum value of the spear, then, will depend upon its productive efficiency. If for some reason which it will be our business to discover, the spear-maker will not consent to barter his spear for something less than the increased quantity of product which it enables to effect, there will be no demand for it, and it will cease to be made. This is a matter of such common experience that it scarcely needs to be enforced. But what is it that will govern the minimum value to which the spear can fall? Here we are on more difficult ground, and shall have to pick our way most carefully.

Let us confine our attention for the present solely to the exchange ratio between spears and the product of the hunt. In the first place, we are assuming that the spear-maker has equal freedom of access with the rest to the hunting grounds; and we are assuming further—no large assumption in the conditions under review—that his skill as a hunter is somewhere about equal to that of the others. Let us suppose that he can produce, and dispose of, ten spears per day. If he chose to remain a hunter, we may, after allowing some portion of the day as necessary to be devoted to the making of a spear for his own use, put down his capacity as a hunter at eighteen units. Hence, an exchange of the spear for two of the hunters' units will bring him an income of twenty units per day—two more units than he could have got by hunting. Nothing less than that will satisfy him, since he can secure an income of eighteen units by hunting for himself. If for any reason—*e.g.*, as a result of competition among spear-makers—the value of the spear should fall for any length of time below two of the hunters' units, some of the spear-makers will forsake the occupation and go back to hunting.

But there is yet another element in this equation which must by no means be left out of the account. The exchange value between the two must have some definite relation to the quantity of effort expended respectively in their production. If, in order to produce the quantity named, the spear-maker has to work half as hard again, or half as long again, as the hunter, or *vice versa*, or if one occupation is much the pleasanter, the additional arduousness or unpleasantness will be a factor in the exchange value. Thus, the spear-maker will be satisfied with an addition of two units to his income over that which he could have secured by hunting if the effort demanded in either is somewhere about equal; he may be satisfied with less, or no increase at all, or even some small decrease, if the work is more to his liking. But if the effort demanded in the industry of spear-making is much in excess of that demanded in hunting, the inducement will have to be proportionately greater. In the conditions under review that inducement can only find expression in the exchange value. If for some reason the hunters are not willing to give as much in exchange as will offer sufficient inducement—*e.g.*, if some other equally efficient weapon is invented which can be produced with a less effort—then the spear will cease to be made.

So far, then, we have arrived at this conclusion: (1) Taking the spear-maker's producing capacity as ten per day, (2) the increase in the product of the hunt due to the efficiency of the spear as ten units, and (3) the addition of two units to the income of either as the minimum inducement—figures chosen at random by way of illustration; if, then, we assume (a) equal freedom of access to nature, and (b) equal effort expended in the respective occupations, the exchange value of the spear cannot fall permanently

below two units of the hunters' product, and cannot rise above eight units. If it falls below two, the spear-maker will forsake his occupation and will go hunting; and if it rises above eight, the hunter will have no desire to possess the spear. The disparity between the minimum and the maximum value is, therefore, very considerable.

The disparity becomes even more pronounced if we allow that the spear will last in use for more than one day. Thus, if we take the hunter's point of view, the spear is worth to him eight of his units, multiplied by the number of days that the spear will last, since he will then get two more units per day for consumption than he could have got without it. As against this, it may be borne in mind that the satisfaction of a future desire is never valued at the same rate as the satisfaction of an immediate desire; that payment for future use (otherwise than as interest) implies the existence of accumulated wealth; and that the chance of accident and other unforeseen contingencies play some part in the deal. But even if we grant that the spear will only last for one day, there is still a wide margin between the two standpoints. What, then, will be the actual exchange ratio between spears and the product of the hunt?

Let us first take the case of goods produced under monopoly, or scarcity, conditions. In advanced societies it is very rarely the case that a monopoly in the production of an article can be held by the exclusive possession of exceptional skill of a rare kind. Sooner or later the requisite skill is acquired by others, when the production is thrown into the melting-pot of competition. Here and there a trade secret may be preserved for some time; but generally, the only real monopoly is that which is given voluntarily for a limited period by nations to individuals, in the form of patents, for the encouragement of invention.

The protection granted to registered trade marks, or distinctive names or descriptions, frequently give the advantage of a partial monopoly or relative scarcity ; and under modern conditions, the aggregation of large capitals, trade combinations, control of transport or subsidiary processes, financial riggings of various kinds, legal charters, and so on, frequently amount to virtual or partial monopolies ; but of this further anon. Let us, therefore, see what it is that will govern the exchange value of an article for which the producer holds a complete monopoly. For convenience of expression, I will use the term "price" as standing for products obtained in exchange.

At first glance, it will probably occur to most that the owner will exact the highest possible price that he can get for his monopoly article. But is that so ? The higher the price, the fewer the number of buyers. Once more we will think the matter out in terms of an ideal unit of product. Let us say that the "cost" of producing each article is 4 units. In effect it amounts to this : That the owner stipulates to give to those who have co-operated with him in the production, 4 units of product as their share, taking as his share all units over and above the 4 which he can get in exchange for the article. Let us, then, suppose that he can get as many as 10 units in exchange for it ; but at that price he can dispose of no more than 10 in a given time. He then tries the effect of a reduction in price on the sale. Suppose that by reducing the price to 8 units he can dispose of 30 in the same time, thus netting as his share 120 instead of 60 units. This encourages him to further reduction. He tries the effect of a price of 6 units, and finds that he can now sell 100 in the same time, thus further increasing his income from 120 to 200 units. He then tries the effect of a price of 5 units, but finds that the sale is increased by only another

50, thus reducing his income from 200 to 150. Leaving out fractions, we may conclude that the price of the article will be 6 units. We may put it, therefore, that the price of a monopoly article will settle itself somewhere about the maximum result for the possible output. Let us now revert to our spear-maker. On the assumption that his skill is rare to exclusiveness, the price of the spear will not necessarily rise to 8 units. For one reason and another—they may prefer some less efficient substitute rather than pay that price—some of the hunters will not care to exchange at that rate ; and with the desire of securing as high an income as possible, he will endeavour to strike the best total result for a given time and labour. The price cannot rise above 8 units, but may be anywhere between that and 2 units.

In the case, however, of spears being produced in open competition, and allowing only for market fluctuations from time to time, owing to excess of supply over demand, or *vice versa* (at the then price), we may take it that the mean price of the spear will be two units. If the excess of supply necessitates the selling below that price, some will relinquish, wholly or partly, the industry of spear-making, and go back to hunting ; and when the price rises appreciably above that, owing to the supply falling short of the demand, new competitors will flock to the industry, until the price is again somewhere about the mean. The reader will probably wish to be enlightened as to the meaning of the qualifying words "at the then price" bracketed in the sentence preceding the last. It means that, at any rate in regard to all such things as are commonly objects of desire, the expressions that supply exceeds demand or that demand exceeds supply are quite misleading without that qualification. Take any one example out of many. When there is what we call a depression in trade, goods accumulate on

the shelves of factory, warehouse, and shop. The boot dealer then says there is a greater supply of boots than the demand for them. Does he or anyone else seriously mean to say that there are more boots than people care to use, or that he could not sell them at any price? Of course he does not mean that. As an actual fact, and allowing for comparatively brief intervening periods of adjustment, supply and demand always balance each other. When the manufacturer, merchant, and shopkeeper find that they have an undue accumulation of boots, the price will be reduced in the effort to bring about a balance between demand and supply. If the depression continues, some will go bankrupt, and others will voluntarily go out of the trade, or restrict the output, until finally the balance is struck. When for some reason there is a sudden demand for boots exceeding the stocks on hand at the time, buyers will be outbidding each other; the makers, discovering the state of the market, will deliberately raise their prices to the possible limit, until at last the buyers at the enhanced price correspond to the supply on the market. If the demand continues brisk, others will flock into the industry. At certain quiet periods of the year, shopkeepers have "sales" to bring the demand up to the supply. When, therefore, we speak of supply exceeding demand or demand exceeding supply, we mean that, at the then price, there are either more willing to buy than there are stocks on hand, or that the number willing (or able) to pay the price does not equal the stocks on hand. But the constant tendency is to an exact balance between the two, through a readjustment of the ratios of exchange, and the number of people employed in the production.

The important points emerging from our investigation so far may, then, be summed up as follows: If we ignore for

the moment the question of capital as we understand it to-day, we see that, granted free access to natural resources, and in occupations demanding no more than an average skill such as is tolerably readily acquired in the then social conditions—

1. The ratio of exchange between commodities will be in direct proportion to the effort expended in their production; and this, spite of the fact that at the moment when the exchanges are effected the values are determined, not by the labour expended, but by the actual relation of supply to demand; for the reason that when the exchange value becomes adverse to one set of producers, they will forsake that occupation for another, wherein, for a similar quantity of effort, the resulting income is higher.

2. That in the case of tools, which are only a means to the end of producing commodities, (a) the tool will not be in demand at all unless the increase in production resulting from its use is such as to leave the user a greater quantity for himself after he had given part of the product in exchange for the tool; (b) neither will the tool come into use unless its productive efficiency is such that the user can afford to give in exchange for it a quantity somewhat greater than that which the tool-maker could, with the same expenditure of labour, have secured by engaging in an occupation the same as or similar to the one in which the tool-user is engaged; (c) hence the ratio of exchange between commodities and tools will also be in direct proportion to the effort expended in their production.

3. It follows from these that, in the condition stated—*i.e.*, freedom of access to nature and in occupations demanding no ability of a kind which is sufficiently rare to amount to scarcity—the tendency is for all incomes to be as nearly as possible equal. These are points of exceeding importance, which will be developed further in the following chapter.

CHAPTER III

THE LAW OF EXCLUSIVE ACCESS TO SUPERIOR FERTILITY

WE have assumed a condition of society in which all have equal freedom of access to natural resources. This condition prevails generally so long as man remains a mere hunter and wanderer. But as time goes on, settled habits of life are gradually acquired, tribes remain in permanent occupation of districts, and there develops a sense of tribal ownership in the soil, which they are prepared to defend against all comers. With settled life, and the need for organised defence, comes settled government ; men give obedience to their chiefs and the officers appointed by them ; and with that there soon arises a privileged class, with exclusive proprietary rights. From a sense of collective tribal ownership in the soil of the district, there generally arises a condition of class and individual ownership.

We may suppose, then, that the forests in which game is most abundant are now reserved for the exclusive use of a privileged class—*e.g.*, the warrior caste ; while the rest of the tribe is restricted to hunting in the sparsely-wooded forests and scrub. Assume further that, owing to this restriction, our spear-maker's capacity as a hunter has now fallen to thirteen units, his daily output of, or the

demand for, spears still standing at ten. Under effective competition, the exchange value of the spear will now inevitably fall to $1\frac{1}{2}$ of the hunters' units, since the only alternative occupation open to him could bring him no more than 13 units, so that he is still 2 units to the good by remaining a spear-maker. Thus, while his income is reduced by 5 units, the privileged hunter's income is increased by 5 units. This increase is, in effect, a form of rent.

Our hunter and spear-maker may be taken as types standing for producers of commodities of all kinds on the one hand, and of tools of all kinds on the other hand. For the product of the hunt, substitute the product of the farm, of the mill, or of the workshop ; and for the spear, substitute the plough, the steam engine, or the dynamo. It matters nothing whether the commodity in question be corn or barley, carpets or boots. If the supply of barley is over-abundant in relation to corn, there is nothing to prevent the barley-growers from cultivating corn ; and the tendency in the long run must be to an exchange on the basis of an equality of effort. But if the corn-growers are in possession of more fertile soils than the barley-growers, then, granted effective competition among barley-growers to become possessed of corn, the value of barley will fall in relation to corn. The effective competition among corn-growers to become possessed of barley cannot have the effect of permanently bringing down the value of corn to the effort level of barley, since the corn-growers can themselves grow barley with greater productivity for similar effort.

To make assurance doubly sure, let us restate this in terms of definite measurement. Say that land of average fertility will yield per acre either 40 units of wheat or 60 units of rye, with equal expenditure of labour. Some

of the farmers will grow wheat, while others will grow rye. The inevitable tendency must be for rye to exchange for wheat at the rate of 3 to 2. If, from miscalculation of possible demand, wheat is abundant and rye is scarce, so that the rate of rye appreciates until it is on equal terms with wheat, it is very clear that some farmers will relinquish growing wheat and take to growing rye, since their own land is capable of yielding 60 of rye for the same labour that it takes to produce 40 of wheat, which now exchange for no more than 40 of rye—a clear loss of 20 units. But now take a piece of land of inferior fertility, which will yield no more than 30 of wheat or 45 of rye per acre. If the owner of it grows for his own consumption, his income is manifestly less by one-fourth than that of the fortunate owners of the more fertile land. But supposing he grows rye and wants to exchange some for wheat. To bring his income up to a level with the others, he should exchange at the rate of 45 to 40. But why should any owner of the more fertile land give him 40 of wheat for 45 of rye, seeing that the same effort which took him to produce the 40 of wheat will provide him with 60 of rye? If the supply and demand happen to be in a particular season such that 45 of rye will command 40 of wheat, some of the farmers will simply take to growing more rye and less wheat.

As between the carpet-makers and boot-makers, and as between both of these and the farmers, it depends equally upon freedom of access to the soil and to either occupation. It is not, of course, assumed that the carpet-maker can forsake his loom and the boot-maker his last on one day and become farmers the next day; or that the farmers can forsake their ploughs and incontinently become carpet-makers and boot-makers. If for some reason—sheer lack of discriminating choice or miscalculation—some occupa-

tions are overcrowded and the consequent competition too keen, parents will bring up their children to occupations in which the competition is less keen, and the consequent income higher. It is a matter of economic tendency operating in time. In other words, it is a question of mental forces operating under given conditions, and are subject to modification just in so far as the totality of factors may recast the mental equation from time to time.

In the case of the production of tools, further considerations of exceeding interest and importance are opened up. Since tools have no utility other than as means to ends, their productive efficiency must be interpreted in terms of an increase in the product of commodities resulting from their use; but their exchange value is governed exactly by the same laws as that of commodities. We shall see this clearly if we again translate it into terms of units of products.

Let the average income in the case of commodities produced and exchanged for each other be twenty units for a given time and effort; then, unless the tool can so increase the quantity of product obtained by its aid that the user will have at least twenty-one units for himself, after giving the rest of the product in exchange for the tool, the tool will not come into use, and will not be made.

But since the tool-maker can himself procure an income of twenty units by engaging in any of the many other occupations, it follows that the increase must be such as to allow of an exchange value for the tool such as will provide the tool-maker with an income of not less than twenty-one units for the same time and effort expended. This does not mean, as may appear at first glance, that the efficiency of the tool must more than duplicate the product. Thus, one tool-maker may, with equal time and effort, be

able to keep a hundred producers supplied with tools as required. If, then, the increase is no more than one and a half units for each producer, there is sufficient to provide each one of the hundred and one parties to the co-operation with an income of twenty-one units, and still leave a surplus of twenty-nine units.

Let us now suppose that the productive efficiency of the tool is so great that it actually doubles the production—a supposition not only without the least taint of exaggeration, but which is very much below the actual fact in the case of modern machinery. How will that affect the income of the tool-maker? Why, the law of equal access will operate in just the same way. If the tool-maker has equal liberty to enter the ranks of the producers of the commodity in question (the reader will remember that we are for the present leaving out the question of capital and other conditions making for relative scarcity, the effects of which will be considered in due course), the tendency must still be to equality of income between them, each getting a proportionate advantage of the increased efficiency.

But, the reader will say, cannot all the other producers also take up the industry in which the production has been so vastly increased by the invention of the tool or machine? Just so. They can—and they will; and the result of that must be again to equalise the incomes between them, through the exchange ratios. Thus, the advantage of increased productivity in one occupation, owing to the invention of the tool, will not be appropriated by the inventor, or by those engaged in that industry alone, but will be shared amongst all those who have utilities to exchange. In other words, an increase in efficiency resulting from human ingenuity, invention, or organisation, will tend to a higher income all round; except only in so far as the conditions create monopoly or relative scarcity —what is, in effect, a restriction on freedom of access.

One frequently hears it argued that certain people "deserve" their bigger incomes because of the greatness of their services—meaning that they are morally entitled to it. But whatever the abstract moral aspect, it is quite certain that it does not operate—probably never has operated—as a factor in human conduct in regard to industry. I am aware of no one, present or past, who has abstained from engaging in an industry on the ground that someone has a moral claim to exclusive occupation. The moral claim may be there right enough; but it requires the legal protection or the economic conditions of restriction to make it operative—the Providence plus the well-primed gun.

So far, then, we arrive at the following conclusions :

1. Under conditions of freedom of access, other conditions being equal, the exchange ratio between utilities for which there is a fairly constant demand is governed by the quantities produced relative to the quantity of effort; that this result is arrived at, not necessarily by the conditions operating at the time the exchanges are effected, but by the more distant mental forces operating as motives for inducing men to enter upon, and continue in, certain occupations rather than forsake those for other occupations; and that, as a consequence of this, incomes tend to be equal.

2. But that under conditions in which the more fertile soil is owned by a section, leaving only the less fertile soil accessible to another section, not alone will the incomes of those restricted to the less favoured section obviously be smaller by the fact that the soil will yield less for a given quantity of effort; but the mere fact of that restriction will so operate that, even in the case of those who are producing tools or other contrivances of high productive efficiencies, provided that the requisite skill is of an ordinary

kind and is open to effective competition, the exchange value of their products will be governed, not by the quantity of product in relation to effort involved—not by the measure of the productive efficiencies of the tools which they fashion—but by the amount of income which they could obtain in the alternative occupations open to them under the restricted conditions.

3. That exclusive access to an occupation, whether the restriction is in the nature of a legal protection, or more or less rare ability, or of any economic conditions, has exactly the same effect as exclusive access to fertile soil. They may all be classed under the law which we may call "Freedom of Access," or perhaps preferably "Exclusive Access," as that conveys the idea more clearly; and the advantage resulting from exclusive access in any form is all in the nature of rent, whether paid in actual fixed quantity, or derived by an appreciation of the exchange value of the utilities provided by the "exclusive" holders in relation to a corresponding depreciation in the values of the utilities provided by those whose access is restricted. In other words, rent is the difference between more advantageous and less advantageous conditions. The work of the possessor of ability may be of higher productive efficiency; but if the ability is of a common type it will not help him to a higher income; and when it is of a rare type, the income will have an increment due to its rarity, apart from its productive efficiency, assuming that we had the means in all cases of estimating the measure of efficiency.

There is, therefore, this all-important distinction between individual increase of income and a national increase of income. Individual income may be increased by (1) exclusive access to more fertile soil, by (2) legal and (3) economic restrictions which limit access to certain industries

and occupations, and (4) by ability of a kind more or less rare. Of these, the last is the only one which creates an actual increase in the national income, just to the degree of its productive efficiency. This qualification is by no means a mere formula. Under modern conditions, much of the ability which gets translated into income is by no means an ability which results in the production of any utility whatever. Thus, the ability to invent a machine, or to organise, or keep in working order, a more effective co-operation, may bring about an enormous increase in production; but the ability, e.g., to discern when "stock" is likely to rise, or the ability of the commercial traveller to snatch an order for his firm by getting on the spot five minutes in advance of another traveller, or by coaxing it out with a glib tongue, is by no means a work of production.

Of the other three, the economic restriction cannot be adjudged as wholly unproductive without further discussion, which will be reached in due course; but tentatively the reader may take it that whatever productive efficiency there is in the economic restriction (e.g., aggregation of capital), is really a matter of organising ability, to be classed under No. 4. But the increase in individual income resulting from the first two adds nothing whatever to the national stock of wealth. It is simply a rise in the income of some at the expense of a corresponding reduction in the income of others.

The increase of income in a national sense is the resultant of three factors added to the one primary factor. The primary factor consists in the resources of the soil of a country—in which is included advantages of position, climate, seaboard, harbourage; in short, everything which puts the country in a favoured position for producing things for consumption at home, or for exchanging with

other countries, whether in the form of goods or services. Given the primary factor for what it is, production can be increased by the application of a greater quantity of labour; by the invention, production, and accumulation of tools, implements, machinery, buildings, roads, railways, docks, and many other things which facilitate the production of wealth; and by the ability of its people to organise more efficient co-operation—what is, perhaps, best expressed in terms of physiology, in a more efficient co-ordination of the functions of the organs constituting the social organism.

CHAPTER IV

"INTRINSIC" VALUE—ETHICAL USEFULNESS—ECONOMIC UTILITY—RATIO OF EXCHANGE

BUT for the confusion of thought inevitable when a term is used indiscriminately to express several different conceptions, and the tangle of psychological speculations altogether irrelevant to the economic issue which has been woven around it, there would be little more to add to the elucidation of economic "value." As it is, we must do our best to clear it of ambiguity, and to disentangle it from the excrescences which have grown on to it.

The first thing which the student must learn is to utterly banish from his economic vocabulary the expression of "intrinsic" value. It is difficult to know what conception anyone has in his mind when he uses that expression. Sometimes he means no more than that the article in question has an exchange value in the market—in which case the term "intrinsic" is not alone a sheer redundancy, but is obviously liable to mislead, by the tacking on to "value" of a qualifying term clearly implying something of the superlative. Sometimes it is stated explicitly that a thing may have "intrinsic" value, although it has no price in the market—"valued for its own sake," it is said. This is clearly a confusion of thought, mixing up personal esteem, regard, or appreciation with economic value. I "value" the friendship of certain persons—some friend-

ships I value "very highly." Surely, it would be the most inexcusable looseness of thinking to confuse that value with economic value, look at it from what standpoint you will. Sometimes it is used to distinguish between a more or less ordinary article of commerce and a rare article of high value, as a first edition, a picture of an old master, a Strad, or an antique piece of furniture. It must be admitted that there is lacking a term to convey the exceptional value attaching to a thing solely on account of its rarity—probably the term "fancy" price expresses the sense nearly enough. But, after all, the high exchange value of a rarity—just because it is rare—has its source in the human desire for ostentation. Now, it is difficult to distinguish between the desire for ostentation gratified by possessing a rare old cabinet at the price of 1,000 guineas, an elaborate modern cabinet at the price of 100 guineas, and an ordinary cabinet at the modest price of 10 guineas. The seamstress who puts up a tawdry curtain at her window pays her few pence for it to satisfy a desire for ostentation.

Sometimes, again, you will be told that by "intrinsic" value is meant an article which has the quality of being "useful," as against another which is bought to gratify a mere "fad." This is really the idea conveyed in the last meaning with a slight variation; one is in part useful and in part "faddy," whereas the other is supposed to be "faddy" without the useful. Far be it from me to suggest that the question of ethical or utilitarian usefulness is outside the province of the economist. On the contrary, since it is the business of the economist to discover the laws governing the production of wealth, and the best means of so adjusting the parts and co-ordinating the functions of the mechanism as will eventuate in a maximum of production, it is distinctly and imperatively within his

province to show wherein the production of the more useful is stunted and starved by the efforts dissipated in the production of the less useful or wholly useless. It is true that one is liable to be pulled up by the quite incontrovertible demonstration that, in whittling down usefulness to its extreme limit, one comes upon a border line in which the one merges into the other, where it is impossible to draw a line between the useful and useless. As to that, the reader is referred to our Preliminary Chapter, dealing with definitions. My advice to the student is that, whenever he is met with a poser of this character he should incontinently make his critic a present of the said border line, lock, stock, and barrel, without the smallest reservation. On either side of that line—some distance away, if you will—are the admittedly useful and the admittedly useless. Tell him that your science deals only with the things which lie distinctly on either side of that line, and that he can have all that there lies on the border line to do with as he likes. His objection is such that, if it were valid, reason and science would become impossible. Clear thinking is, indeed, so rare a quality that one is apt sometimes to give up in despair any attempt to make people think rationally. In the term "useful" is contained two quite distinct conceptions inextricably mixed up. Usefulness has no meaning apart from a preconceived end in view, some desired purpose to be achieved—*e.g.*, food to satisfy hunger, clothing and shelter as protection against the elements, pictures and books to satisfy the aesthetic and mental faculties, and so on. "Useful" means, therefore, efficient to accomplish an intended purpose. But tell the man who objects to racing that the racehorse is useful, and he will repudiate it with all his might, although the horse obviously serves the purpose for which it is intended. Indeed, in the mere sense of efficiency,

the poison or the pistol is useful to the suicide, since it accomplishes the purpose which it is intended to serve. What is chiefly meant when it is said that something is useful is, that the purpose which it serves is commendable on some abstract ground. Before, then, it can be agreed that a thing is useful, it must first be admitted that the purpose which it is to serve is approved from an ethical, or national, standpoint. Thus, the usefulness of the racehorse may be disputed—not on grounds of efficiency, which is beyond question, but on the ground of ethics or national service—but there is no room for disputation as to the usefulness of food, clothing, and shelter, since the ethical and national value is not questioned. Within the limits of common consent, therefore, it is by no means outside the scope of scientific conception to map out an approximate classification of degrees of usefulness, from food to silks and diamonds, including the racehorse, if you will. If, in the view of some, "betting" (e.g.) lies right across the line of demarcation, argument is of no avail, since no acceptable conclusion can follow except from admitted premises.

But if the term "value" is to stand for ethical or utilitarian usefulness, we shall want another term for expressing the exchange ratio between things. It is clear that the market price of things does not correspond to an ideal classification of utilitarian merit—e.g., the price of the diamond will stand higher than the loaf of bread, and the price of the racehorse will stand higher than that of the carthorse, preach as energetically as you may. If it were attempted to measure exchange value by some ideal classification of usefulness, we should soon loose ourselves in a most hopeless quagmire. Whatever thing or service has an exchange value must be assumed to satisfy some desire; but whether the desire is one to be commended or

deprecated is quite another matter. By the production of "utilities" the economist means, therefore, things and services which satisfy human desires; and by "value" he means the ratio at which they exchange one for the other. If the quality of exchange value attached to material substances alone, there would be no need for the term "utilities"; we could then speak of them as "things." But since an untold number of intangible services also satisfy desires and have exchange value—as the services of the preacher and the teacher, of the singer, the musician and the actor, of the administrator and the organiser, to say nothing of the millions of intangible services incident to the production of commodities—the term "utilities" is a most convenient expression for signifying the wider conception. Together with the term "value" and many others, it suffers from the ambiguity and looseness inseparable from colloquial usage. At any rate, I am not responsible for the choice.

The term "intrinsic" is sometimes used to exclude that part of the market value of a business or other undertaking which is based on an estimate of probable future profits—which we call the "goodwill" of a business, or the price of a complete or partial monopoly. By the "intrinsic" value would then, I take it, be meant the bare value of the building, stock, etc., if sold as a piece of movable property—say a piano or a sideboard; while its value as an *exclusive* profit-yielding concern—a profit which, it is presumed, could not be secured by putting up a similar building and stock elsewhere, at any rate not without involving the uncertainty and risks attaching to an effort to build up a new business, or that profit due to a still more exclusive monopoly possession, such as the profits of a railway, a tramway-track, a water-supply, and so forth—is held to be, presumably, an "artificial," but not an intrinsic, value. But there

is very little reality in such a distinction. The value of anything and everything really depends upon an estimate of future profits, if we interpret profits in the true economic sense—*i.e.*, the right to the enjoyment of utilities. If a house is bought for investment, the purchaser bases its value on the future rent it will yield him; and if he buys it for residence, the value is based on the rent it will save him—a distinction without a difference. If he buys a piano, he estimates its value by its future use as compared with what he would have to pay for the monthly hire of one like it. If he buys furniture, he estimates its future use as compared with what he would have to pay for renting a furnished house or apartments. We have called the added value attaching to a commodity or service produced under "exclusive access" a form of rent; and if the term "artificial value" will better express the fact, I can see no objection to it. We are concerned about clearly defined thoughts, and not with the word symbols used to represent them. But even so, that would not make the use of the term "intrinsic" any the clearer. Then it is said that a house may have a market value because it will yield rent, though from the health point of view its "intrinsic" value may be less than nothing. This simply takes us back to the idea of expressing value by a preconceived standard of usefulness, only, as we have seen, to land us in an impenetrable swamp.

Sometimes the term "intrinsic" is used to denote the metallic value of "token" money—silver and copper in this country—as distinguished from their nominal value; and similarly it is used to denote the metallic value of a debased coinage—*i.e.*, either deliberately tampered with, or worn down by abrasion. I think these two—particularly the last—are the nearest approach to a useful employment of the term; yet I see no reason why it cannot be equally well expressed by "metallic" value.

Finally, the expression "intrinsic" is used to differentiate between a "commodity" currency, gold and silver, and a paper currency. The metal currency is said to have intrinsic value—*i.e.*, value for use in the arts apart from its use as a tool or medium of exchange—whereas the paper currency is practically a wholly ideal contrivance (the minute cost of paper and printing may be ignored). The subject of money or currency will form no inconsiderable part of our investigation later on. For the present it is sufficient to say that the difference is best expressed by calling the metal currency just what it is—a "commodity" currency, or as having commodity value. It matters little, indeed, what terms are used, so long as they express clearly defined thoughts, and serve the useful purpose of cutting one conception clear from another. But the term "intrinsic" is used in many senses, and, indeed, appears to have no clearly conceived thought behind it. Even where it approaches some clearness of conception, it is wholly unnecessary, and can only serve to mislead.

In the first place, then, let us get hold of the general principle which operates to induce men to give up something which they possess in exchange for another thing which they desire to possess. The totality of man's desires is, of course, not a fixed quantity. In a general way, he desires to possess everything obtainable; at any rate, everything which will yield him satisfaction in possessing. They may be things for the satisfaction of physical needs, or they may be for the satisfaction of mental desires, in which may be included the motive prompted by sheer vanity, by the mere fact that it is possessed by others. The woman will hanker after a hobble skirt, or the man after a Panama hat, not because of any reasoned concep-

tion of beauty or comfort, but because it is supposed to be in the fashion. With the change of fashion there is a change of desire, the fashions frequently working out a complete cycle.

But it so happens that, with the exception of air, sunshine, and beauty of landscape, nature yields nothing to man without labour. Even air, sunshine, and landscape cannot be obtained by many town dwellers without labour given in exchange for the facilities of occasional visits to country and seaside. Dwellers near rivers can sometimes obtain drinkable water with the minimum effort of fetching. Certain wild berries, fruits, and edible vegetables, may be obtained in some sparsely-peopled parts of the world by the mere effort of picking; but in most cases the effort of reaching the spots and of picking equals or exceeds the effort of cultivation. For practical purposes, then, we may say that nature will give nothing to man without labour; and, conversely, that labour applied to land—meaning by “land” all that it contains on the surface and buried beneath the soil—is the only factor capable of yielding to man the means of satisfying his desires.

We need not labour the point that, in giving up the product of his effort in exchange for the product of another man's effort, man will endeavour to give as little as he can, and get as much as he can. Ethical considerations of equity do enter to some extent in advanced societies; public opinion and custom have a controlling force in certain human relations, and are to that extent modifying factors; but the primary motive is to economise one's labour. Exchange value, then, is an obvious consequence of labour expended. Man will give nothing for what can be picked up for nothing. At the moment of exchange, it will be a question of giving as little and getting as much as one can.

We are already sufficiently familiar, I trust, with the main causes operating in the adjustment of values—the ratio at which things will exchange for each other. The main source of confusion arises from an inability to appreciate the difference between an immediate and an ultimate cause. The producers of utility “A”—call it corn—desiring to become possessed of utility “B”—call it barley—will endeavour to get as much as possible of “B” for as little as possible of “A”; but the producers of “B” will endeavour to do exactly the same thing in regard to “A.” The actual ratio of exchange will depend upon the quantity of “A” seeking to be exchanged for “B” in relation to the quantity of “B” seeking to be exchanged for “A.” In other words, if corn happens to be scarce in relation to barley, the producers of barley will be bidding against each other to become possessed of corn, until an equilibrium is established between the relative supply and demand on both sides. The same thing will happen if, though the actual quantities remain as before, the desire to consume corn has increased, while the desire to consume barley has decreased. But the very same desire to economise one's labour—to get as much and give as little as possible—will operate ultimately to a readjustment of the conditions within the limits open to the respective producers. If the land used in the production of barley can be employed with equal advantage for growing corn, the owners will take to growing corn, until the increased quantity of corn in relation to the diminished quantity of barley brings about a new equation. If the land employed for barley cultivation will produce a less quantity of corn for effort expended (or, which comes to the same thing, an equal quantity but of inferior quality), so that there is nothing to choose between the greater quantity of barley at a lower value and the smaller quantity of corn at a higher value,

then the owners of the inferior soil will have to be content with a smaller income, or work harder, or both. If a fashion has set in to wear sandals rather than boots, the bootmakers will take to making sandals; but if sandal-making has been made a legal monopoly, then the bootmakers must either forsake their trade for another or be satisfied with a smaller income. The utility for which the producer has a complete or partial monopoly—whether it be due to special ability, or to legal restriction, or to exclusive command of economic advantages—will command a higher exchange value in relation to non-monopoly utilities, just in proportion to the extent of the desire for its possession.

But this brings us to the somewhat baffling psychological question of "desire," which will require careful consideration. True, the value depends upon the relative quantity of supply to demand at the time of exchange. But demand is only another way of expressing desire to become possessed, so that the quantity demanded means in effect the extent of the desire. Now, it should first be premised that economics is not, *per se*, a study either in psychology or in ethics. In so far as the mental forces are operating factors in production—and that is to a great and constantly increasing quantity—we are bound to study the psychology of the mental phases; in so far as the misapplication of energy into vicious channels hinders the production of wealth, we are concerned with the ethical aspect; but we are not concerned with the abstract philosophy of either science beyond its direct application to economics.

Now, to start with, our conception of quantity of desire shares in common with our conception of any other quantity in nature that it conveys nothing intelligible without a comparison. A distance of a verst conveys nothing

intelligible, unless you know what relation it has to a foot, a yard, or a mile. A mass of a pound conveys nothing intelligible, without you know what relation it has to an ounce, a pound, or a stone. Indeed, quantity *per se* has no meaning to us otherwise than as related to something of greater or less quantity. But, at any rate, magnitude and extension may be taken as something definite and constant in nature, even though they convey nothing to our intelligence except as compared to some other quantity.

But in the case of a human desire, not only can we have no approximate conception of its intensity except as related to other desires either more or less intense, but in many, if not most, cases the desire which becomes translated into action is only just strong enough to overcome other desires in the opposite direction. Whatever may be the case in the field of religion and ethics, in the field of economics action is practically in every case the result of a balance struck between opposing desires. With every change in economic conditions, with every change in environment, there is a recasting of the balance between desires.

Are we, then, in a position to say that value is an index to the intensity of desire? If, to avoid redundancy, we allow ourselves prematurely to express it in money terms, this would mean that the desire to possess a Gainsborough at £80,000 is just 640,000 times as intense as the desire to possess a loaf of bread—a preposterous proposition on the face of it. To begin with, the comparison is here between a satisfied desire and an unsatisfied desire. If the owner of the gold were in a starving condition on an uninhabited island, and the captain of a passing ship offered him the choice of a Gainsborough and a loaf of bread at £80,000, there is little doubt that the choice would not fall on the Gainsborough. If the comparison is to be valid, it must

be between two equally unsatisfied desires. The main point is that the value at the moment of purchase is not a simple expression of an intensity of a desire, but is the expression of a choice between alternative desires. The poor housewife will pay fourteenpence a pound for butter, not because fourteenpence is the exact measure of the desire, but because she prefers that to the next alternative choice of margarine at tenpence, or the next-but-one choice of jam at sixpence. To that extent we are entitled to postulate a graduation in the scale of satisfaction derived. If butter goes up to sixteenpence a pound, she may prefer the margarine at tenpence; or if the margarine falls to eightpence, butter remaining as before, the desire to save the sixpence may lead her to prefer margarine to butter. The equation struck between alternative desires which finds expression in a given choice is a resultant of three factors; the income at the disposal of the chooser, the desire to economise, and the desire to consume. As between the choice of an expenditure of £80,000 on an estate, a Gainsborough, or building a hospital, there is a comparison of desire; but it is idle to compare the unsatisfied desire of possessing a Gainsborough or a castle with the satiated desire of having a dinner.

The intensity of desire varies with individuals, and almost from moment to moment with the same individual. Many a man will forgo a meal to have a smoke, and many a woman will half starve herself to obtain finery. At all hazards, we must strictly guard ourselves against mixing up desire, so far as exchange value is concerned, with an assumed classification of usefulness. By a desire we express a condition of mind operating at the moment the exchange is effected; whereas a postulate of usefulness expresses a permanent standard of ethical or utilitarian values, in a gradually ascending scale, corresponding to

the scale of values. We know that this correspondence is not true in fact.

But while the desire to consume is operating as a factor—in proportion to the general standard of income—to increasing demand, thus tending to outstrip the supply on offer at the then value, and so raising the value, the opposite desire to economise one's labour—in other words, to increase one's income by the relative appreciation of one's product in relation to the product of others—is constantly operating in the opposite direction. No sooner does a relative scarcity set in in the production of any utility, with the consequent rise in value, than those whose products stand at a lower value will either themselves launch into the industry the product of which is relatively scarce, or will put their children to it. In so far as there is freedom of access, utilities will tend to exchange effort for effort, and incomes will tend to be equal. Where the utilities stand at high values, and the consequent income is higher, it is purely the result of exclusive access, whether by means of actual restriction in access to soil, or economic condition, or by ability of a rare type.

Value in economics, therefore, expresses a "ratio of exchange" between utilities, but does not express an abstract conception of value. Like any other expression of quantity, it conveys nothing that is intelligible except in relation to a larger or lesser quantity. The money terms only duplicates the process of comparison. Thus, a pound of jam at sixpence, a pound of bacon at a shilling, and a pound of tea at eighteenpence, have respective economic values as 1:2:3. A "macute" may be an unknown quantity to you; but if you are told that a given quantity of jam is one macute, the same quantity of bacon two macutes, and of tea three macutes, you know that tea

is three times the value of jam, though you know nothing of the macute. Without the comparison—the ratio between two or more utilities—value in economics is meaningless. A person may attach a great deal of that "value" which is meant to express personal esteem to an autograph of a deceased parent; but if the autograph has no exchange value in the market, the economist is not concerned with it, nor has he the means of knowing its relative intensity. The possession of it may be wealth to the owner, but it is not wealth in the economic sense. Behind the exchange value the economist is bound to assume a desire satisfied; but he is content to—he has no choice but to—take the exchange value as indicating the quantity of desire as related to other desires either more or less intense for the time being.

Finally, a few words as to the enormously high values of rare objects. So far as the laws governing values are concerned, there is nothing further to be added. They are just articles of monopoly which, owing to the impossibility of increasing the production by even a single addition, the inducement to a reduction in value operating in the case of other monopolies is completely absent, hence the highest obtainable value will be exacted. But, in common with other luxuries of high value, they indicate an enormous increase in human capacity to produce wealth, with enormously increased incomes to the holders of exclusive possession of factors which are in the nature of monopolies or scarcities. Generally, it is expressed as indicating a great accumulation of wealth; but, as used in this connection, it is largely a sheer illusion. It is not the accumulated wealth that really pays for the luxury, but the utilities created from day to day. We shall develop the meaning and consequence of this as we proceed with our investigation.

CHAPTER V

MONEY AS THE MAGIC TALISMAN—WHAT PAYS FOR LUXURIES

We must yet for some time longer follow the fortunes of our ideal, self-dependent tribe, in order that we may, from the simple conditions before our mind's eye, be able to see standing out clearly and distinctly certain economic issues which, under the complex conditions of modern industry, become blurred and confused to obliteration. Indeed, if the student is not to lose himself in the maze of modern conditions, and still more so in the almost impenetrable jungle of modern terminology, he should make it a point of keeping a clear mental picture of the simpler state from which the more complex has grown, and of reverting to it on all possible occasions of doubt and perplexity for reference and verification. New conditions bring about new mental and social equations, but whether the conditions are inevitable for all time, whether they conduce to the best economic results, is quite another matter. Certain essential principles remain to-day just as they were under the simpler economic adjustments, but are merely buried under an avalanche of illusory conceptions and terminology, only to be disinterred by a patient analysis into the simpler elements.

Our ideal tribe has been making rapid progress, and is now entitled to be called a nation. The discovery of the

art of smelting metal inauguates a new era ; man steps out of the "Stone Age" into the "Iron, or Bronze Age." Many new tools are invented, many contrivances for the economising of labour thought out, and specialisation grows apace. New handicrafts spring into being, and with a wider outlook and higher ideals the desires are multiplied and take on greater intensity. Some genius discovers that clay can be made to retain a permanent shape by baking, and the art of pottery-making comes into being. Some notions of spinning, weaving, and tailoring are gradually developed. The art of agriculture is all the time being slowly evolved, and stock is vastly improved by selective breeding. A few of the more venturesome make their way to the far-off coast, where they discover some prettily coloured shells, which prove to be much in demand as ornaments. The desire for the decorative and artistic becomes more general and more intensified.

As yet, there is little differentiation between landowner and worker, and capitalist and worker. Everyone is still a landowner, or has access to land and forests owned in common ; though, in the very nature of the case—since all land is not alike in fertility and advantage of location—some must be restricted to less fertile soil than others. The landowner is still a worker, and the artificer owns his tools and works in his own home. Factory and workshop life in the sense in which we know it has no existence. Of capital there is little beyond the simple tools of the farmers and artificers, and the rooms and outhouses necessary for carrying on the industries. Even shops for the aggregation, display, and sale of goods has not yet come into vogue.

So far the inter-tribal trade is of very small dimension. Tribes are separated by long distances. Of roads in the modern sense there are none, communication is difficult

and hazardous, and loads have to be transported, sometimes on the backs of animals, but not unfrequently on human shoulders. For practical purposes, each tribe or nation is self-dependent and self-centred. The members of the nation make up between them a complete circle of producer-consumers. Their ideas of needs and desires soar but little beyond the producing capacity of the members of the tribe. By bartering with each other, they manage to satisfy their simple needs. What barter is done with neighbouring nations is carried on by what we should call general merchants—merchants who do not specialise in one or two particular products, but who become the medium or agents for bartering all the surplus products of one nation for the surplus products of other nations.

As habits of industry grow, as man's efforts become progressively more productively efficient, owing to the invention of tools and the better dovetailing of parts—the more effective co-operation—labour can be spared for road-making and for improving the village or town. As the pressure for satisfying the mere needs becomes lessened, thought is given to the provision of comforts ; and when these are provided, with labour still to spare, the desire for the possession of luxuries can be satisfied.

This idea of labour adjusted on a graduated scale for providing needs, comforts, and, finally, luxuries, will, I am afraid, appear to the reader as some fantastic notion out of "*Alice in Wonderland*," being well aware that it has no correspondence to the actual world of reality as we know it. Not only is it not true that men are engaged in the production of luxuries as a consequence of the fact that there is already an ample provision of necessities, but the truth seems to be the exact opposite : that the consumption of luxuries at one end is in exact ratio to the

absence of provision for satisfying needs and comforts at the other end. Nay, the law operating appears to be just the other way about ; that even the meagre provision of a miserable subsistence for many depends largely upon, and is a direct consequence of, the production of luxuries, useless freaks, and the pandering to all sorts of vices. Unfortunately, this is a perfectly true conclusion in no small measure under the present economic condition, but is to be interpreted in a special sense, as we shall see in due course.

Now, this is just one of the economic tangles which it is our business to unravel. Its full significance cannot be made clear until we are farther advanced in our investigation ; but we are in a favourable position for getting at least a glimpse of the truth while yet our minds are fixed exclusively on a self-dependent economic unit, carrying on their exchanges by means of pure barter. As we proceed, it is hoped that the student will have succeeded in completely shaking off that conception which interprets the economic mechanism in terms of a magic talisman—money—which somehow materialises utilities from the infinite vastness of nowhere ; that his mind will have been thoroughly attuned to conceiving the problem in terms of production of these utilities by human hands and brains. This is a task which is not to be accomplished by a mere explanation, however convincing. A mental conviction, ingrained from childhood and strengthened and fortified by daily impressions through a long course of years, is not to be wiped out by an argument, like sponging writing off a slate. Intellectual assent alone is not sufficient. The impression has to be eradicated by a course of mental discipline sufficiently prolonged to overcome the inertia which is as true of mental as of physical habit. A few moments' filing may suffice to take out a lightly scratched

impression on a metal plate ; but if the characters are deeply engraved on hard steel, the work of obliteration may occupy many hours. Indeed, one is often tempted to the conviction that nothing less than a miracle will ever succeed in eradicating the economic impression.

I was told the other day of a racing tipster who employs twenty clerks, and spends some thousands annually in advertising in the sporting papers. The listeners consisted of a number of people employed on "press" work ; and, when I remarked upon the lamentable waste of human effort, I was met with the rejoinder that it provided a living, or some part of it, for a number of people—the clerks, the compositors, the stereotypers, the machinists, the engineers, the publishers, to say nothing of the paper-makers and dozens of others to whom it gave employment directly and indirectly. In a leaderette in one of our daily newspapers, commenting on the Registrar-General's report of a diminution in crime, the editor concluded his remarks by saying that even the black cloud of crime was not wholly without a silver lining, since it provides employment for policemen, jailers, magistrates, judges, *et hoc genus omne!* Instances could be multiplied by the hundred. Now, it is scarcely to be credited that the writer in this newspaper of huge circulation did not pay lip homage to the formula that "money is the medium of exchange," or, indeed, that he did not really grasp the purport of that formula. And yet, that obviously did not help him to shake off the crystallised conception that money-getting is the end of employment, regardless of whether it is productive or unproductive—even to conceiving crime not to be without its uses, on the score that it provided employment for which money was paid.

This critical digression will, I trust, help us to a more ready understanding of the point under consideration. By

narrowing down the problem to a self-dependent community, practically isolated from the rest of the world, the issue before us will stand out in clear and bold relief. Wealth, we say, can command luxuries. But there is one thing it cannot do : it will not enable one to eat the cake and keep it too. No one has yet discovered the secret of getting more oil out of a cruse than it contains. The luxury producers must have necessities—food, clothing, and shelter—if they are to go on producing; and that food, clothing, and shelter which they are consuming must of necessity be produced by others. If the accumulated wealth should consist of a store of necessities, the luxury producers may be kept provided while the store lasts; but, in the first place, many eatables will perish if stored up for any length of time, and, in the second place, that provision can only be of a temporary nature. If the luxury production is to remain a permanent occupation, the saved-up store must be continually replenished; so that we come back to our proposition that the existence of luxury production of necessity postulates that others must be continuously producing the necessities which are consumed by the luxury producers. There is as yet no magic talisman to summon utilities from the vasty deep of nothingness.

We are not in a position to carry the analysis farther until we have reached a more advanced stage in our investigation. For the present, it is sufficient if we but get an inkling of the truth that money does not provide luxuries—that, indeed, it provides nothing beyond the tool or contrivance by which the exchange of utilities is facilitated. A mountain of gold in the possession of the would-be consumer will not provide him with a single utility unless the food, clothing, and shelter necessary for the maintenance of the producer of that utility is being

produced by others from day to day. An individual in the midst of a nation of producers, or a nation in the midst of other nations of producers, may command some utilities which they desire in exchange for stored-up actual wealth (utilities) which others desire to consume; but this can only be a matter of short duration. It is not, therefore, either money or accumulated wealth that commands utilities. It is the resources of a country, plus the producing capacity of its people, that provide the utilities. It is the continuous effort of producing from day to day which is the magic talisman that calls utilities into being—not the money, which is only the token whereby each is apportioned that share of the product which the economic conditions enable him to exact. The recent two great strikes (Railway and Transport Workers strikes in 1911) have made most of us realise of how little avail is money and saved-up wealth in face of the paralysis which overtake a nation by the stoppage of even one important branch of production.

The reader may, perhaps, think by now that the matter is altogether too obvious to need all this elaborate argument. If, as I devoutly trust, this is his present view, I can only congratulate him on the advance he has made in economic conception. Already he is miles ahead of the editorial economic conception which can see a modicum of virtue even in crime, because it enables some people to earn money. But let him not be over-confident. Even writers on economics have not escaped getting entangled in the meshes of their own terminology, mistaking the shadow for the substance. It is all plain sailing while our mind is fixed on a simple economic adjustment; the confusion of thought will come when we get into the exceedingly complex mechanism of the modern industrial state.

CHAPTER VI

DIFFICULTIES OF BARTER—A CURRENCY CREATES
A REVOLUTION IN MECHANISM OF WEALTH
PRODUCTION—CURRENCY IS A CREDIT ON THE
COMMUNITY IN GENERAL

THE difficulties of barter depicted in the textbooks are fairly familiar ground. The classic illustration of the tailor who, having a stock of coats on hand, has yet to go shoeless because he cannot find a shoemaker who happens to be in need of a coat moves us to commiseration. When, after tramping the round of the shoemakers, he at last discovers one who is in need of a coat, his troubles are by no means over. If the value of the coat is equal to four pairs of shoes, how is he to barter if he wants no more than one pair? Well, at any rate, the shoes will keep; but the poor fellow is driven to utter despair when he wants a loaf or two, and has nothing but a coat to offer in exchange, which equals the value of eighty loaves. Since the loaves will go stale and mouldy long before he can consume the lot, he has apparently the unenviable choice of starvation on the one hand or black ruin on the other. The baker or butcher who wants a coat or shoes is faced with exactly the same dilemma.

The state of chaos conjured up by this picture had no counterpart in real fact. It is much more true to say that the gradual evolution of a currency gave a corresponding stimulus to the arts of production, than that the absence

of a currency made exchanges of commodities and services a practical impossibility. Put in another way, that production which is apparently impossible without the aid of a currency is in itself a direct outcome of the invention of a currency. Within the narrow limits of the small national unit and the primitive state of the industrial development, man had early in his career devised means for exchanging utilities without the aid of a tangible currency. There are unmistakeable indications that, long before a currency transferable from hand to hand was invented or thought of, our primitive ancestors had already, in some degree, stumbled upon the true solution of the currency problem which, after many thousands of generations, the modern world is evolving at the present day. In the time of Homer, values were computed in terms of oxen, but it is very obvious that the oxen did not pass from hand to hand as payments for goods and services. No other currency is mentioned, and the conclusion is irresistible that the ancient Greeks had evolved a system of credits, the oxen merely serving to express the unit of value, and as ultimate security for the liquidation of debts, something analogous to our bank reserves. The credits were probably personal as between the parties to the exchange, but enforceable by law. But I fear I have allowed myself to anticipate far beyond the stage reached in our investigation.

Nevertheless, the inconveniences of barter, even with the aid of personal credits and some recognised unit of value, were real enough; and they kept on becoming increasingly so as man advanced in the arts of producing wealth. Division of labour in the production of a single commodity is the most essential factor to a progressive increase in production. But in proportion as division and specialisation took place, the need of a currency became more and more pressing. Not one of the producers had anything

tangible to barter, since neither of them had made the commodity outright, but each performed just one operation and passed it on to the next, until it finally got shaped into the object ready for use. As man began to produce things which required united and prolonged effort before they could be materialised into objects of utility, the need of some tangible instrument or token which shall register the value of each worker's contribution to the productive effort, entitling him to draw some stipulated quantity out of the general stream of products, became imperative. And so man muddled somehow into inventing a currency.

With the history of that invention we are not concerned, beyond a knowledge of such facts as will throw light upon the real meaning and function of money. In the course of its evolution, a great multitude of things have been used, and are now being used, as money. Thus, cowrie and haiqua shells, skins, leather, sheep, corn, maize, olive oil, cocoa-nibs, tea, tobacco, salt, clay, iron, lead, and tin have been used as money. As has already been mentioned, Homer expresses the value of things in terms of oxen, saying of certain things that this was worth so many oxen and that so many. At a somewhat later period, the money at Carthage consisted of leather discs, in which something was sewn up, though no one knew what it was—an astute confidence trick, apparently, of the then Chancellor of the Exchequer. At Lacedaemon iron was used as money. In Ethiopia they used carved pebbles as money. "Among the Indians in New England wampum was used as money. In German New Guinea the bent tusks of a boar are used as money. In California red birds' heads have been used in the same way. Stone money and shell money are used in Melanesia. In Burma Chinese gambling counters were used as money. Gutta-percha tokens issued by street car companies in South America

are said to be used in the same way. Not many years ago in a town in New York State, similar tokens got into circulation, until their issue was forbidden by the United States Government. In Mexico large cocoa beans of relatively poor quality were used as money, and on the west coast of Africa little mats were so used" (Professor Irving Fisher, "The Purchasing Power of Money.") The reader need scarcely be reminded that inconvertible paper is used as money in several countries.

The use of purely token money, such as the Carthaginian leather discs, indicates a high degree of mental and industrial advance. There is little doubt that the earliest form of money consisted of some object much in demand as a commodity for ordinary use; the probability being that more than one such commodity performed the function of money at the same time, until, by a gradual process of selection and elimination, the one that performed the function most efficiently displaced the others. The primary function of money—the one, at any rate, that is the most obvious—is that of enabling exchanges to be effected of things of unequal value. Thus, if some sort of shell, obtainable only by a long and arduous journey to the far-off coast, was much in demand for ornament, our classic tailor would readily barter a coat for a number of these shells; not with any intention of presenting them to his wives and daughters to be used as ornaments, but so that he may barter them away, as need arose from time to time, for such small things of daily use as he may require; feeling convinced that he would have little difficulty in finding bakers, butchers, and grocers ready to take the shells in exchange for their wares. Perhaps he would as readily barter the coat for little mats or baskets if he thought that the demand for these sundry articles was about equal. But in course of time, experience proves

that one of these serves the purpose more efficiently than the others. The shells, for example, may prove relatively in greater demand than the mats or baskets ; or, if the demand for them be about equal, the shells may be much more convenient for the purpose, on account of their small individual value, which enables them to be bartered in various quantities, extending over a wide range of values. But our tailor is not the only one to discover the service which the shells are capable of rendering in this way. The baker and butcher who accept them in exchange do so for exactly the same purpose—so that they may, in their turn, exchange them with others for whatever they may need. And so in course of time the shells become money before even people have formed a clear conception of the meaning of money. From being taken as a more or less readily exchangeable commodity, subject nevertheless in some degree to a search for buyers, they gradually come to be accepted as a matter of course, and, without question, in payment of goods and services. Once such general acceptability is firmly established, the commodity in question becomes true money.

The use of money having become firmly rooted within the minds and habits of the community, it rapidly becomes a factor of enormous magnitude to a profound and far-reaching modification of the whole economic structure. The problem of currency is one of baffling complexity ; but we shall get at the solution all the more effectively if, instead of grappling with it by a frontal attack—if one may be allowed a military simile—we follow our hitherto method of gradual conquest from the outworks to the citadel. In other words, instead of launching straight away into an investigation of the nature and function of the modern monetary system, and attempting to analyse it into its constituents, we shall do better to possess our

souls in patience while we review some of the immediate and more obvious consequences of the establishment of a currency simple and direct in its operation.

We may now picture our ideal nation to have completely acclimatised a shell currency, which is accepted without demur in payment of goods and services. The quantity of the particular kind of shell available for use—in part as money and in part as ornament—may be assumed to be of just that degree of scarcity which renders it suitable for the purpose ; and it further possesses the quality of durability, together with a considerable degree of divisibility—owing to its small individual value—two qualities which are essential to a lasting currency. Granted the requisite degree of scarcity, and the possession of a commodity value, as being in demand for the purpose of ornament, such a currency is in every respect but one very nearly equal to a gold, platinum, or silver currency. It fails only in the respect that, unlike metal, it is not capable of being cast into varying quantities at will, to represent a graduated scale of values. But this is a matter for further consideration. At any rate, our nation is now completely equipped with a full-blown currency capable of meeting their economic needs. The existence of an established currency soon brings about changes of stupendous magnitude both in the mental and economic conditions of the social organism. We must now do our best to trace the nature of those changes, and to evaluate as accurately as may be the causes, direct and indirect, which are at the basis of those changes.

Under conditions of direct barter, production is rarely carried appreciably beyond the barest of necessities, or at most to the extent of a few comforts of an elementary type. This is due primarily to the fact that the cumber-

some and inelastic barter process is so extremely ill-adapted to co-operation in production—by which I mean the unconscious co-operation between separate industries, not the modern, organised co-operative partnership of a particular industrial unit. Take the case of our classic tailor as an illustration. Even under relatively simple conditions, the tailor's product, as we understand it to-day, is the result of a co-operation between several industries. He is directly dependent for his raw materials upon the weaver; and the weaver, in his turn, is dependent upon the spinner; and the spinner is dependent upon the sheep-breeder; to say nothing of intermediaries for collecting, transporting, and distributing the materials to their various destinations.

Now, let us see how the barter process will work out between the various agents in this series of co-operation. As between the tailor—the vendor of the finished product—and his customers, the process is relatively simple. The farmer who wants a coat bargains with the tailor to give him so much of his farm produce in exchange. It does not necessarily follow that the tailor will take away the stipulated quantity of product in bulk. The matter can easily be arranged on a credit basis—say a daily supply of so much corn, eggs, milk, and butter for a given period. With the butcher the tailor bargains for so much meat; with the shoemaker for so many pairs of shoes; with the pottery-maker for so many pots and pans; with the mat and basket maker for so many mats and baskets. But how does the matter stand with the weaver? He also wants corn, eggs, milk, butter, meat, shoes, pots and pans, mats and baskets. But his only customer is the tailor, and he produces none of these things. Beyond an occasional supply of a coat, the tailor has nothing to give that is of any use to the weaver. The spinner and breeder are faced with exactly the same dilemma.

It is true that in the value of the coat is embodied also the labour of the weaver, spinner, and breeder. Currency or no currency, in the value of the finished commodity is always contained the exchange equivalent of all the labour that had been expended in its production throughout the whole series of processes that it had passed through, subject to more or less temporary market fluctuations; and it is the final consumer of the commodity who has to give in exchange for it the full equivalent of all the labour effort that had been put into it. To make the matter quite clear, let us express it once more in terms of ideal units. Suppose that the breeding of the sheep requisite to produce a given quantity of wool necessitates the expenditure of 100 units of labour; that the spinning of the wool involves the expenditure of another 100 units of labour; that the weaving it into cloth involves another 100 units; that the making up of the cloth into coats means yet another 100 units; and that the resultant product of all these processes materialises into 100 coats. If, then, we assume an exchange under freedom of access, the consumer of the coat will have to give in exchange for it something in the production of which four units of labour has been expended. The modifying conditions due to restriction of access, and the fluctuations owing to supply and demand, have already been dealt with in preceding chapters. Thus, if the tailor's trade is relatively scarce, the value of the coat may be something which equals five units of labour, of which the tailor may get two units, while the other contributors to the total result will get one unit each.

But though the coat will command the value of all the labour put into it throughout the various processes, the difficulty of apportioning and distributing the product for which the coats will exchange amongst the various factors

is practically insuperable under barter. If we imagine a consciously organised co-operative partnership between the various agents whose labour contribution goes to the final emergence into being of the finished coat, then the mere distribution of the products for which the coat will exchange amongst the various parties to the co-operation may, perhaps, be manageable. But who are to be the parties to the co-operative partnership? As between the spinner, weaver, and tailor, the intimate relationship of their occupations may make a partnership quite practicable. But what about the breeder? His connection with the spinning, weaving, and tailoring trades goes no farther than the supply of the wool. But over and beyond that, he has the carcases and skins to dispose of. By the former he is co-operating with the butchers, and by the latter he is co-operating with the tanners, shoemakers, harness-makers, and several other trades. If his breeding is not confined to sheep alone, or if he is engaged in general farming, then he is further co-operating with many other trades. But the spinning, weaving, and tailoring trades are not confined purely to woollens; flax, cotton, jute, and other fibres are also spun, woven, and made up into cloth and wearing apparel. Thus a great many other industries are drawn into the circle of co-operation. The work of collecting the small quantities of materials in their various stages of preparedness from the scattered producers and transporting them to convenient centres may be a matter of little moment within the confines of a small community; but it becomes a matter of constantly increasing importance as the nation grows in numbers, in geographical area, and in industrial development. Then there are the makers of buildings, tools, and other implements without which the production of commodities could not be carried on—the providers of the "capital" of industry. All these are co-operating in the production of

the coat. Under modern conditions, it is scarcely possible to find any trade or occupation whatever which is in any real sense independent. Even the gatherer of groundsel and wild flowers uses a basket to carry them in, and thread or wire for tying up the bunches—materials which have passed literally through hundreds of processes, perhaps even thousands, before reaching the final stage of consumption. While, therefore, barter between those employed in the final processes—*e.g.*, the baker, tailor, and shoemaker—and the actual consumers of the commodities may be managed with some little ingenuity, in part on a credit basis, the apportionment and distribution of the products for which the commodities will exchange between all those engaged in the intermediate processes, who are not in touch with the actual consumers, presents difficulties of a magnitude manifestly insurmountable by any ingenuity short of the invention of some instrument which gives the holder an undisputed claim on production in general—virtually a certificate of the community's indebtedness in return for services rendered—be the instrument gold, silver, nickel, or shell money, leather discs or pieces of paper. The money problem will be considered in due course. Pending further investigation, the proposition may be emphasised that the essential quality of money is, that the claim which it constitutes shall be "undisputed,"—that it shall be generally accepted in payment without question or demur.

In absence of such an instrument, the co-operation of many in the production of a single commodity—the splitting up of the work into separate processes divided between as many groups of workers, the finished commodity emerging only as a result of the final process—was a matter of practical impossibility. As a consequence, division of labour to any appreciable extent was out of

the question. Such occupations as became specialised were generally of so simple a nature as to admit of all the necessary work connected with it being performed by the artificer and his family. Thus, *e.g.*, the carpenter would cut down himself what timber he required; the potter would dig up his own clay; and the mat and basket maker would himself collect the rushes or strip the bark requisite to his trade. Spinning and tailoring would be done by the family in their own homes. The weaver would simply bargain to weave the yarn supplied to him into cloth, thus dealing direct with the actual consumers. Such conditions of industry are by no means absent amongst rural communities in various parts of the world even to the present day. In short, while co-operation in the sense of a reliance one upon the other for the interchange of various products and services is an inevitable condition of human advance beyond the mere brute *existence*—the hunting and cave-dwelling period—the co-operation in the production of commodities is in the main a direct outcome of the invention of money.

The adoption of a currency creates a complete revolution in the entire mechanism of the production of wealth. It now becomes possible to split up the production of a commodity into sundry processes, divided between many groups of workers. In effect, as will be elucidated later in more detail, men discharge their services into a vast pool of co-operative effort where, after a more or less long series of metamorphoses, they finally emerge in a stream of utilities ready for consumption. Except only those who are employed in the very final process—the actual distributors of the finished products—no one has anything consumable to barter. Instead, each contributor to the pool receives a check or token—in the form of the currency of the country—which gives him a valid claim to draw

from the stream some stipulated quantity of finished product, of such value as the economic conditions enable him to exact.

Our breeder, spinner, weaver, and tailor are now in a position to co-operate together, without getting into an inextricable tangle as to the manner in which each is to come by the share due to him as the exchange value of his contribution. The exchange process is now of an entirely different nature. The farmer will get his coat, and will still give for it as much corn, eggs, milk, butter, etc., as the exchange value of all the labour put into the coat can command in the given conditions; but it does not follow that either the tailor, weaver, spinner, or breeder will get any of that particular farmer's produce. Indeed, the produce which is to form the exchange equivalent of the coat had already been given up by the farmer some time before he gets the coat, and had, perhaps, long since been consumed. But in return for having allowed others to consume the product of his labour, he received a floating credit, or claim, in the form of so many shells, entitling him to demand from others a certain equivalent. He now transfers that floating claim to the tailor in exchange for the coat, and in this way obtains the equivalent to which he became entitled as a result of having previously given up so much of his produce to be consumed by others. The change in the process is threefold: (1) The actual barter is duplicated—goods into shells and shells back into goods; (2) the process is in effect a system of credits; (3) but instead of each transaction being between an individual debtor and an individual creditor, as is the case with ordinary credit instruments, the currency gives the holder a credit on the community in general—whether tacitly, by custom, or explicitly, by legal enactment, is not material so long as it remains effective—and the community

in general becomes the debtor, giving the holder of the currency the right to tender it for all goods on offer to be exchanged—what we should now call “on sale.” In his turn, the tailor who receives the shells from the farmer gives up a number of them to the parties who are co-operating with him, retaining such share for himself as the economic conditions enable him to exact. In due course, these various holders exchange the shells for such utilities as they may require; and those to whom the shells are transferred in exchange for the various utilities become again entitled to demand coats in exchange for the shells. In effect, it is the same old barter, but in a more or less roundabout way.

In actual fact, it may be that the tailor will have to keep a sufficient stock of shells on hand to pay the weaver before he had himself exchanged the coat with the farmer; and the weaver may have to keep a stock on hand for paying the spinner before he had exchanged with the tailor; and the spinner may have to keep a stock for paying the breeder or the producer of the vegetable fibre before he had exchanged with the weaver; and all of them may have to keep a stock on hand for paying wages—a subject which we shall reach in due course. In so far as the provision of such a stock of currency is necessary for the efficient accomplishment of the process, it has to be paid for as a necessary tool of exchange—just as the hunter will give some part of his product in exchange for a spear, or the carpenter a part of his product for a plane, not because either the spear or the plane is in itself a desired object of possession, but merely as a means to the end of increasing production. In effect, those who are engaged in the industry of shell-collecting are provided by the rest of the community with various utilities, to such exchange value as their services will command, in return for providing a

tool which, by facilitating exchanges, enables production to become vastly more prolific.

As a result of the facilities which the exchange medium affords for subdivision of labour in the production of single commodities and for a wide co-operation between separate industries, not only is man's capacity for producing wealth vastly increased, but, in course of time, it effects also a profound change both in the whole structure of the social organism and in the mental attitude and outlook. The nature of these changes, and their effects for good or evil to the race, we shall develop as we proceed with our investigation.

CHAPTER VII

CHANGES DUE TO CURRENCY—SAVING: "REAL" AND "PERSONAL"—ECONOMY MEANS INCREASED PRODUCTION FOR LABOUR EFFORT—INTEREST

HAVING reached the stage of an established currency, the questions relating to it and the consequences flowing from it crowd upon each other in such hopeless profusion, and present issues of such exceeding complexity, that it becomes very difficult to deal with them in orderly and progressive sequence, and quite impossible to deal with each point adequately. The issues involved in the money problem will come up again, and yet again, in much more complex and obscure forms; and it is, therefore, all the more essential to the understanding of the problem that we should preserve, as much as possible, a progressive order in the development of our subject.

Of the very beginnings of currency we know nothing; but from what we know of the introduction and development of currencies amongst primitive peoples, even at the present day, we can form a fairly accurate notion of the process. Our classic tailor, making up into clothing the coarse homespun produced in the farmers' and hunters' cottages, finds himself one day hard driven to procure food. He bethinks himself of offering to exchange some strings of shells, which in his more prosperous days he had presented to his wives and daughters to wear as ornaments,

and finds the farmers quite willing to barter. When next the wave of prosperity returns, he seeks not only to replace the shells he had bartered away, but endeavours to increase the quantity as a stand-by against such an emergency as he had experienced; on the same principle that many of the poor in our towns buy massive wedding-rings—not unfrequently several rings—so that in case of need they can be pawned for an appreciable sum. Repeated experience of this kind, not confined to the tailor alone but to many others, at last places the shells in the position of a favoured commodity, into which people convert their savings; and from that it finally assumes the character of money accepted as a matter of course in payment of goods and services; to which there is later given, perhaps, also a legal sanction. The cowries having become the accepted currency, our working tailor gets his payments now in money, instead of in kind.

There happens to be one family, we may suppose, exceptionally clever in weaving cloth of good appearance and texture, which becomes the talk and envy of the district. Many of the more prosperous farmers then endeavour to procure the cloth in exchange for farm produce, rather than wear the coarse stuffs which their women are capable of turning out in their own homes. Thus both farming and weaving get well on the road to becoming specialised industries. The farmer gives more of his time and attention to producing more and better crops, some of which he will need to give in exchange for the cloth; while the skilful weavers in the end give up farming altogether, and rely for procuring what they need of farm produce and the raw materials of their trade in exchange for their skill as weavers. As a consequence, greater proficiency is acquired, and much labour is economised in both trades, resulting in increased production.

In course of time, one of the tailors discovers that he can secure for himself a bigger income by keeping a stock of the cloth so much in demand, thus placing himself in a position to bargain for supplying the clothes outright, instead of working up the materials provided by his customers. Our tailor has now become a "capitalist" in the commercial sense that we use it to-day. (In the strict sense, practically everyone engaged in any industry whatever is a "capitalist" of a sort, even if his capital consists of nothing more valuable than the iron hook of the wool-comber or the shoulder-pad of the fish-porter.) In effect, a system of co-operation is set up between the farmers who produce the wool and fibre, the spinners and weavers, and the tailors.

The establishment of a system of credits by means of a currency is the principal factor in bringing about, in course of time, changes of enormous magnitude : (1) in man's efficiency as an individual producer; (2) in the unconscious co-operation by the division of production into many processes performed by different groups of workers, resulting in a vast increase in production; (3) in conscious co-operation and organisation of industries into large units under central control and management, resulting in still further increase; (4) in enabling production to be localised to favourable soils, climates, and other conditions, with the same result; (5) in the ability to produce and accumulate tools and other implements of production, and the erection of buildings and other works of magnitude which further add to human efficiency as producers; (6) in the ability to undertake work of experiment and research, which, when successful, enable us to harness natural forces to human service, make new products available for consumption, and render human efforts vastly more prolific; (7) in the facility it affords for undertaking work of a

public character, national and communal; (8) in profoundly altering and intensifying the incentive to a higher standard of living, and to "saving"—the most potent factor in human progress—resulting in the development of habits of steady and strenuous application; (9) and in gradually re-constituting the social and economic fabric in many ways, until finally the conditions which we know as "Freedom of Access" ceases to have more than an academic significance, applying only to ideal conditions which have no longer any existence in old countries, or, at any rate, exist only in a very limited and relative sense. All these, whether for good or for evil, could not—in absence of universal integrity—conceivably have come about without the intervention of a "medium of exchange" in some form.

At the outset, it is necessary that we should get some clear notions on the vitally important subject of "saving"—a subject that will frequently come up for further consideration. In the whole range of economic thought, there is scarcely a more striking example of a term which habitually conveys a conception so utterly at variance with the economic reality; and even where the conception has some approach to the reality, it is lamentably lacking in clearness and definiteness of outline. Saving is nearly always conceived in terms of money. Where one's possessions consist of land, houses, shops, factories, mines (other than for personal occupation, business, or trade), or in any other form of property whatsoever, people will say that his savings are "invested" in such and such property. The actual "savings" is the money; the factories, mills, machinery, houses, and other forms of durable property are merely the things in which the real savings are invested. Now, it requires but little serious thought to realise that the act of "saving" consists in preserving

something in being that might otherwise have been consumed or destroyed. If you rescue anyone from drowning or from a burning house, you have "saved" a life that might otherwise have perished. If you pack away your suit for the coming summer, you preserve in being clothes that might otherwise have been worn out before then. The peasant who stores away at harvest-time corn in the communal granary for seed in the coming spring is "saving" the corn from being consumed by the family in the stress of winter shortage. Saving, in short, in the economic sense should mean preserving some consumable thing in being to be used for future consumption, either as a commodity or implement to facilitate production.

But money—considered as money and not as a commodity, as, *e.g.*, gold to be used as jewellery, plate, or door-handles, if you like—is not in itself an object of consumption, otherwise than as a tool for facilitating exchanges. Mountains of it would not sustain a single life. Considered directly as an object for preserving in being, the accumulation of actual coin or bullion beyond the minimum required to carry on the exchanges, instead of being a gain, is a sheer waste of human effort, and a useless tax on the community—as would be that of employing men to build machines, factories, and other tools which are not required to be employed in production. Money is no more than the token representing a claim in return for utilities given up to be consumed by others. We shall realise this all the more clearly when we come to deal with modern currency, when we shall find that, instead of saving so much of actual coin, what has been saved is nothing more tangible than credit entries in books.

But even indirectly, the fact that money (*i.e.*, credits in

any form) has been saved does not necessarily mean that anything consumable has been preserved in being for future use. True, the possession of money registers the fact that goods or services have been rendered by the holder, or by others on his behalf; but it does not follow that the goods or services rendered for the money materialised in anything of a more or less enduring character. The utilities given up for the money may long since have been consumed—perhaps in the very act of rendering, as the services of the singer, actor, or musician—and the utilities for which the money will ultimately be exchanged may as yet not have been produced. It has been aptly put in the form of a paradox that "what is being saved has been consumed." But that is, of course, not necessarily the case, and is purely a question of fact. Our classic tailor might have consumed in food, drink, and other things, the full exchange value of the whole of his product. If instead of this he exchanges for general credits on production, some of which he puts by for future use, whether anything has actually been saved is a question of fact.

If the clothes which he has produced, and for which he has as yet received no equivalent in other utilities, went to keep in health and working efficiency a number of men who were employed in building a bridge, or an aqueduct, or a workshop or factory, or in constructing a road or a railway, or in any other work of an enduring nature and utility, the money represents actual saving. Something has been created and preserved in being which, but for the provision made by the tailor and many others, would not have been in existence at all. The process of vicarious saving need not have been so direct as that; and may be ever so much more roundabout. The clothes may have gone to clothe some farmers, who in return provided the

food to maintain the workers ; or they may have gone to clothe some miners on another continent, who produce the iron ore which, after passing through many processes, and over long distances, finally became the pickaxes which the workers used in the construction of the road or railway. We shall become more familiar with the dynamics of such complicated industrial mechanism as we proceed. But if the clothes went to maintain non-producers, or producers of something that is of no real service—shall we say those who set up the type and print the racing tipster's advertisements?—then his money-saving represents no real saving, and may be even injurious rather than beneficial. But even if the tailor's product should have gone to clothe those engaged in making something durable that is intended to be employed as an instrument of industry, if it should happen to have been made in miscalculation of the actual needs, and should prove to be derelict, then nothing really consumable has been created, and there is no actual saving. It is all, as has been said, purely a question of fact.

But though the money may not represent actual saving, the possession of it makes a world of difference to the owner. The fact that A has a right to demand utilities from B, C, and D cannot make the nation as a whole any the richer. If anything, the nation must be the poorer by the fact that some of its members may be called upon to give up their products to be consumed by non-producers. But to A, the possession of those claims is a matter of great moment ; and the saving of them an economic reality of immense consequence. By abstaining from consuming the equivalent of the whole of his product—what we should call his "earnings"—allowing others to consume those products, services, or utilities in exchange for valid obligations to render an equivalent on demand, he provided for the proverbial rainy day. To him, the saving is real

enough, whether or not the products with which he parted in exchange for money have been so utilised as to result in the creation of some product, physical or mental, of more or less enduring utility. Allowing that the claims consist of nothing more tangible than entries on a banker's books, there is still all the difference in the world between using up those claims in the present, and that of leaving them to be used on some future occasion. It is idle to tell the owner of the claims that he has effected no actual saving ; he has saved the claims instead of exercising them and consuming the proceeds, thus providing against future need.

This apparent conundrum is nothing more than an absence of terms for expressing two distinct sets of facts, and what should be two distinct conceptions. The least thought must make obvious the sharp distinction between the accumulation of things actually consumable, whether commodities or implements, and that of claims on production. The mere claims of A on B to Z to provide him with utilities add nothing to the quantity of utilities in existence. If those utilities produced by A (or by others on his behalf) in return for which the claims were given consisted of something enduring, or went to maintain workers who were producing something enduring, then, though the claims are not in themselves real saving, they represent something actually saved. But there is nothing in the claims themselves to show whether they stand for something actually saved or not. And yet, to the holder, the claims are "saving" in the sense in which we understand the word, since he could easily enough have consumed the whole equivalent of his product from day to day—as we should say, he could have spent all the money he earned ; whereas he chose to forgo that satisfaction, preferring to consume less than he might, and "save" the

claims for future demands. How, then, shall we distinguish between these two kinds of "saving"? I confess my inability to invent appropriate terms, and can only ask the reader to classify them mentally by the qualifying descriptions of "real" and "personal"—the former standing for actual things saved, and the latter for money or claims in any form.

We are now free to revert to our merchant tailor, who now contracts to provide the coat outright, instead of working up the materials supplied by his customers. In the first place, we are bound to conclude that he sets up as a merchant tailor with a view to increasing his income. In order to procure and lay by a stock of cloth, he must first of all "save." But saving can only be effected by one of two means: one must either work harder and produce more, while consuming as much as before; or else, while producing no more than formerly, one must consume less, denying oneself the satisfaction of many legitimate and habitual desires, so as to leave a margin of "saving." In brief, saving can only come as a result of producing (by self or proxy) more than is consumed (by the actual producers or those entitled to the product). Now, there is clearly no point in our tailor doing either of these if his income is to remain what it was. Why should he either work harder or skimp and deny himself things with the object of employing his saving as a trade "implement"—for that is what the saving so employed comes to—if he is to earn no more than he could formerly by working on his customers' materials?

But a bigger income in the case of producing and selling goods can also come by only one of two ways. It can come by way of an enhanced value of the goods, or by way of economising labour; and, of course, by both these

ways. If we assume freedom of access to the trade, we are bound to conclude that there will be no appreciable rise in the value of the coat, for the obvious reason that other tailors would offer to continue on the old method of making up the customers' own materials. The condition of freedom of access does not long remain in full force after capital has stepped in as an important factor in production; but that is a matter which will be reached in due course. The increase of income must, therefore, be attributed rather to the economising of labour. We may suppose that, under the new conditions, the customers go to the tailor's shop to be measured. Thus, there is economy of time previously consumed in searching for customers, in fetching and carrying the cloth, and so forth. There is time saved in having the work under one roof, continuous and ready to hand, enabling a more perfect organisation and dovetailing of the various parts. There are similar economies in the case of the weaver, who now has to serve only one customer—the tailor—in place of, say, a hundred of the actual consumers; and this enables him to reduce the price of his cloth to the tailor. The net result of these economies is an increase in production for labour effort. The exchange value may, then, indeed fall and yet leave a bigger income to all parties concerned in the production.

The student should make it a special point of thoroughly familiarising himself with the conception that "economy in cost of production," if it is to have an economic reality, must mean "increase in production for labour effort." The economy in money cost may or may not represent increased product for the same amount of labour. The employer may economise by reducing the wages of his employees. Assuming for the moment that underpaid labour is as efficient as well paid, the quantity of product available for consumption will then remain as before. The

only economic effect will be that the workers will be reduced to a lower scale of consumption ; while of the products which they are creating more will remain to be consumed by others. That is simply a change in the "sharing out." You cannot call that a real "economy" which merely takes from Peter to give to Paul. Or the employer may exact from his employees longer hours or more strenuous effort for the same wages ; in which case there will be added product (at any rate for the time being, though not, perhaps, in the long run), but not an increase in relation to labour expended. The only real economy is where, by means of more efficient tools, a more effective co-operation by those engaged in the different processes, a better organisation and co-ordination of parts in individual industrial enterprises, more is produced for the same expenditure of labour. The money economy then represents a real economy.

It is, however, well to remember that it is possible to produce more for the same labour effort and yet leave the total quantity of product no more than it was before. Thus if, by better organisation or the introduction of machinery, an employer can make three hundred workmen produce as much as four hundred did before, if the hundred workmen now in excess of that required to produce the same quantity of goods are merely turned adrift as unemployed—thrown on the scrap-heap, as it were—there is no increase in product ; that is to say, there is no increase in total product in relation to the total number of people desiring to consume the product. Of course, if you eliminate the now unemployed as no longer within the circle of consumers—as merely so much rubbish—as something which is of no earthly or heavenly concern to those within the circle—there is a decided increase, inas-

much as there is now available for the consumption of three hundred an exactly equal quantity to that which previously had to be shared out amongst four hundred. (Whether the actual workers would get the whole or any of the additional product is another matter—the increase is there.) There is an increase even if you do not allow the derelict hundred to starve to death, but maintain them on a pittance in the form of charity or legal relief (generally conceived as charity), in so far as the product remaining for the consumption of those within the circle is now greater in quantity than when the four hundred workers had to share equally. It is simply a question of a point of view. If you take into account the nation as a whole, then an increase in production must mean that there is more produced per head, or a greater total product, than there was formerly ; and real economy does not consist in the employer merely getting so much for less money, but in so organising the industry that more is produced for the same labour effort. The main cause, then, of our tailor's increased income will be due to the fact that the new tool—the capital which he now employs in his industry—enables him to produce more with no greater effort ; and that each increment of labour employed results in a larger production than could have been obtained without the aid of capital.

I say the "main cause," but not necessarily the only cause. The student should always be on his guard against hasty generalisation. He should realise that several causes may be operating to a given result ; and that the proximate cause is by means necessarily the same as the ultimate cause, as has been explained in our discussion on values. In the case under consideration—as, indeed, in practically all cases—the immediate cause of an income higher than the average is due to what may variously be defined as

"Exclusion of Access," "relative scarcity," or "partial monopoly"—all meaning practically the same thing. Under "Freedom of Access" the tendency is always, as we have seen, to equality of incomes. You have only to imagine every actual and potential tailor to be possessed of the requisite capital to realise that, spite of an increase in productive capacity, the increase would soon be given away to the consumers under stress of effective competition, until the income of the tailors was somewhere about the level of incomes obtainable in other industries. Of course, increase of production all round would mean increased income all round. If, then, the tailor producing with the aid of capital obtains a bigger income than the working tailor struggling on under the old conditions, the proximate cause is simply the fact that the capitalist tailor has access to conditions of production from which the working tailor is excluded. But the ultimate cause, nevertheless, is that the production with the aid of the credit-tool results in more product for the same labour effort. In other words, the "exclusive access" is the proximate cause, but it is the "superior fertility" which is the ultimate cause. There is a bigger income because there is an increase of product—that which constitutes real income—owing to the access to the means of increased productive capacity reserved to the few who are in possession of the tool which makes that increase possible. Allowing for time and trouble saved to the consumer, in obviating the need of first going to the weaver to buy the cloth and then taking it to the tailor—in reality a part of the increase in productive capacity for labour effort—it may be taken generally that the consumer will not consent to give more of his own product in exchange merely for the sake of dealing with the capitalist. But if the exchange value is to remain somewhere as before and yet yield a bigger

income to the capitalist tailor, it must be because labour is economised by means of working with the new tool. The ultimate may, however, be the same as the proximate cause—*i.e.*, there may be an increase in exchange value, with or without an increase in production—where conditions approach more nearly to complete monopoly, whether from patent rights, large combines, excessive capital, trade secrets, very rare talent, or any other unique advantage.

The bigger income accruing from the employment of capital is said to contain an item of "interest." But apart from direct lending at interest—as banking, money lending, and investing in interest-bearing securities—the allocation of so much of the profit of trading as interest is a purely arbitrary distinction. The trader will make as much profit as the conditions of the trade will allow him to make; and these conditions, subject only to accidental variations, are without exception the measure of the "Exclusion of Access," in which is included special ability and aptitude for the business. When the business has to pay interest on borrowed capital, the interest is simply so much of the outgoings; the payment for the use of the tool without which the business could either not be carried on at all, or not so productively. The allocation of so much of the income as interest has a real significance in so far that a manufacturer or trader would not permanently carry on an enterprise which yielded a smaller or no greater income than could be obtained by lending the capital out at interest. Nay, we can go much farther, by saying that he would not consent to remain permanently in a business which yielded a less or no greater income than others in which less capital is required. Sooner or later the business would either be relinquished, or adapted and organised on new lines, so as to yield as good an

income as other enterprises employing the same amount of capital.

The subject of interest has given rise to much discussion most of it of extreme futility; but none so utterly futile as the conundrum, "Is one morally entitled to charge interest on capital?" As we have seen, so far as concerns the capital directly employed by the owner in production, the value of the product or service is not governed in the smallest degree by a consideration of interest, either as an abstract moral claim or a plain business consideration; except only in the insignificant negative sense that the producer will not remain permanently satisfied with an income no greater than could be got by investing or loaning the capital out at interest. It is governed, as we know, by a much wider law: proximately by the exclusive access, or relative scarcity, which is given to the enterprise by the employment of capital, but ultimately by the economy of labour effected by the use of an efficient tool; subject, however, to the exception that where the exclusion amounts to a practical monopoly, what we know as the proximate may be the only operating cause—in other words, the product may command a high value relative to labour effort not because of, or to the extent which, it would consume more labour if produced by any other means, but because the means of producing it at all, or of a sufficiently close or acceptable substitute, are difficult of access, or are entirely inaccessible, to any but the present producers. One may have invented a machine or other contrivance which increases production a hundredfold, but if he has no means of restricting access to it, the value of the product will be governed by the remuneration or income of labour effort in other occupations to which there is similar freedom of access; and where restriction of access is secured, it is rarely indeed that the inventor gets the advantage of it.

If moral claim were the ruling consideration, I wonder what the descendants of the inventor of producing fire artificially could claim by way of royalty? And what if they claimed arrears also!

Leaving out of consideration extortionate interest, mainly a consequence of human folly and improvidence, the temptation to engage in an argument in defence of commercial interest is considerable, were it not so useless a piece of casuistry. Since money, or credit in some form, is admittedly an indispensable factor in production, it follows that he who provides one of the necessary tools, thus co-operating in the production, will get a share of the produce, whatever the casuist may urge to the contrary. It is indeed difficult to find the dividing line between an increase of income due to the employment of one's own capital, and that increase due to the employment of borrowed capital. If the owner of the capital is entitled to it in the one case, why not to a share of it in the other case? And what of the income which is wholly due to the borrowed capital? Modern business is nearly all done on credit; and though the merchant who gives the credit may not classify his income under the separate heads of profit and interest—though the economic law does not depend on either, but is the result of Exclusive Access—yet that portion of the increase in income which is due to the relative scarcity of the capital which enables one to give credit practically amounts to interest on the loan. In what essential does that differ from a loan of money or credit when not coupled with active business?

"Interest is the reward of abstinence" is a phrase in frequent use, meaning thereby the abstinence which is the condition precedent to saving. The subject of saving will further engage our immediate attention. The phrase is true enough in fact, provided we do not understand the

term "reward" in the ordinary acceptation of a deliberately designed means of encouragement, in the same sense, e.g., that a schoolboy may be rewarded for good conduct or diligence, or a soldier for an act of bravery, and so on. It should be understood as the economic condition automatically, as it were, creating the inducement without which the capital—which is the result of abstinence—would have no existence. Interest will in that sense be the additional income which one is enabled to earn by carrying on industry with the aid of capital, which forms the inducement to saving. No one portions out, or plans out, the reward; it is merely the economic result of employing a more efficient tool, which can only become at by means of abstinence—by producing more than one consumes, thus leaving a surplus for the creation of capital. The fact that some save, while others do not, creates that exclusive access, or relative scarcity, which is the immediate cause of the increase of income.

We are not sufficiently advanced in our studies to follow appreciably questions relating to banking and currency; yet, a certain aspect of the objectors' case makes a brief reference to the subject desirable at this stage. It is held by some that our present system of banking (the principal money-lending organisation) and the provision of currency is made an artificial monopoly. As we shall see later, the bulk of the money of commerce is provided by a class of money-dealers; which money, moreover, consists in the main of nothing more tangible than pieces of paper and entries in books; and the necessary managing and organising ability is merely acquired as a trade, but is by no means of a rare type. Granted, it is urged, that the remuneration is the result of given economic conditions, that is no reason why the conditions should be allowed to

remain an artificial monopoly—that there is no sense in using an expensive tool when a cheaper one will do the work equally well or better. The carpenter wants a plane with a good blade, but there would be no sense in setting the blade in a platinum block, when a wooden or steel block will do the work as well. Why should a few privileged people be able to draw a considerable share of wealth as remuneration for the exclusive management of the currency in their own way, when it could really be organised on a different and more economical plan with better results? In that sense interest becomes immoral, inasmuch as the conditions are "rigged" to create a scarcity, which enables the monopoly-holders to exact a reward not warranted by the inherent economic conditions. Such, in brief, is the position of more than one school of currency reformers. The subject is one of exceeding complexity, and this brief mention of it is all that we dare venture upon at the present stage.

CHAPTER VIII

CHANGES DUE TO CURRENCY—THE ECONOMIC UNIT—
OPERATION OF ECONOMIC PROCESS—COLLECTIVE
AND PRIVATE ENTERPRISE—THE EFFECT OF SAVING—
ECONOMIC SURPLUS

WITH the firm establishment of a currency as representative of utilities given up to be consumed by others, and constituting a valid and undisputed claim on the products and services of others, man's economic conception and outlook gradually assume an entirely new aspect, giving rise to mental and, in course of time, physical changes of the most momentous consequences. Under a state of barter, exchanges are practically confined to parties mutually desiring to consume each other's products. The horizon of demand is, therefore, very limited, and readily definable. The work of the "distributor" has not become specialised to any extent worth mentioning. There is no "market," in the sense of buyers to sell again. Every operation of barter involves a search after the actual consumer. Nature, with her varying moods and violent contrasts, is the spiteful step-mother, taking delight in spoiling her step-children's handiwork, whose spite may sometimes be turned by propitiatory sacrifice, but for the rest must be submitted to with the resignation of fatalism. With no evident means of wresting from nature what she is apparently unwilling to give, ambition to economic advance remains

undeveloped. The mental vision projects little beyond the immediate present.

A currency having come into being, the boundaries of the mental horizon are rapidly extended, and ambition to attain a higher standard of comfort soon takes the place of slothful resignation. The mental factor begins to play an important part in the economic mechanism. Middlemen who act as distributors spring into being. An open market for the disposal of products of all kinds is ready at hand. The economic unit is rapidly widened. In place of each village being dependent upon its own resources and effort for the production and interchange of all the things which go to satisfy their needs, the currency provides the means of exchanging with other villages. This enables production to be specialised to localities. Thus, if the soil of one village is more suitable for growing barley, while the soil of another is more suitable for growing maize, maize will go out of cultivation in the one and barley in the other. By "more suitable," one means, of course, that more (or of better quality) is capable of being produced for a given effort. In this way, the quantity of product is increased, and each village has more of both products than it could have done by producing the two on its own soil.

The operation of the currency will, perhaps, be more clearly visualised if we present it in this wise: By an "economic unit" we will mean a village, town, district, or country whose people interchange utilities one with the other. Under modern conditions, practically the whole world is one economic unit; but that was not always so. For the purpose of our illustration, we will conceive an economic unit of small dimensions, consisting of the individuals, or groups of producers, A to Z. Between them they produce the various things necessary to satisfy each other's needs. They constitute, therefore, what we

shall know as "a circle of producer-consumers." A has given up something to be consumed by Z, for which he received some shells or coins, representing a claim to a given value as equivalent. A, then, tenders the money in satisfaction of a utility which he obtains from B. But why, you will ask, should B satisfy A's claim for something consumed by Z? To which the answer is that he doesn't. B cares nothing for A's claim; but he takes the shell or coin simply because he knows, or believes, that it will, in turn, be accepted by others in exchange for such utilities as he may require. When a currency gets out of order, as it sometimes does, and confidence in its ready acceptability is shaken, the claim which it represents will not avail. B then gets something from C, C from D, and so on, until finally it gets back to Z, and the circle begins afresh. Within that circle there is, we will suppose, one individual, Z, engaged in collecting the shells required to perform the function of currency. In return for providing that necessary instrument, he gets his share of the utilities produced by the other members of the circle, to that extent which the value of his services will command in the economic conditions. The reader will, no doubt, see here much that requires further elucidation; but this we shall reach in due course.

The establishment of a currency soon creates an entirely new conception of the economic process—an utterly false conception, but one which, nevertheless, has played a part of supreme importance in the economic development of the race. Confined to exchanging by means of direct barter, the producer can see an evident limit to the usefulness of his activities—the end of his tether is too obviously within sight. If he is a farmer, he knows from experience that by growing more farm produce than he needs for his own consumption he can exchange the surplus for boots,

coats, mats, and other things produced within his narrow "circle of producer-consumers"; but he is not keen on wearing out more boots, coats, and mats than are necessary to meet his usual requirements; and has decidedly no ambition to lay by a stock of these relatively perishable things for a rainy day. His own product is practically beyond the capacity of being saved at all. If he is the boot-maker, tailor or mat-maker, his capacity for saving is equally circumscribed. Beyond some few simple necessities, wealth among primitive peoples is practically confined to cattle—the only stock that renews itself without loss. The ambition to "save," remaining undeveloped, there is no surplus available for the maintenance of those whose labour might have been devoted to the creation and accumulation of "capital"—a term the full significance of which we shall realise more fully presently. The economic process is interpreted for what it actually is—*i.e.*, that men are engaged in producing utilities for consumption—but there is nothing to indicate the vast potentialities of man's producing capacity (*a*) under changed conditions and organisation, (*b*) with the aid of better tools and implements, and (*c*) with the addition of the mental factor developed by experience and education.

The general claim on utilities which the money constitutes creates a new mental outlook. Industry is seen as a means to the end of getting money—men work only because, and only to the extent, that it happens to be the way to obtain money. The money, in its turn, commands utilities of the most diversified character. The introduction of a currency—which, as we know, is both the effect of the necessity created by the division of labour, and the cause of rapidly bringing about a further and more elaborate sub-division—results in a great increase in production. More things are available for consumption; there is a

greater variety of products on the market; all of which are offered for money. What, then, can be more obvious than the fact that money is the magic ring which calls things into being? I was about to remark that the people amongst whom money first came into use were not very expert in tracing effects to causes; but I am frequently led to doubt whether, *relatively to the data at his command*, modern civilised man (if we leave out the few specially trained in scientific demonstration) is not less capable of logical deduction than was even his primitive ancestor. At any rate, it would seem certain that he is less capable of concentrating his mind on one issue at a time, there being apparently a pronounced tendency for ideas to spread out and evaporate into all sorts of side issues of little or no relevance to the point under demonstration.

With the new mental outlook on the one hand, and the wider range of utilities within reach on the other hand, desires multiply and increase in intensity. "Saving" assumes a new meaning, and offers an apparently unlimited scope. Apart from the economic illusion, there is an obvious attraction and advantage in saving something which commands utilities of all kinds at sight, to be exercised when and how one likes, to the saving of more or less perishable things, strictly limited in their uses. But since there is no means of saving otherwise than by producing more than one consumes, the desire to save results (a) in a progressive increase in production, (b) the development of habits of industry, (c) the exercise of mental ingenuity to economy of labour in production, (d) all of which result in setting free a stream of products available for the maintenance of others who can now be set either to producing "capital" or luxuries, as the case may be. To whatever extent the saving becomes embodied in

"capital," the capacity to produce wealth is increased; in some cases multiplied many hundredfold.

Accustomed as we are to the complicated mechanism of the modern economic process—particularly those of us who live in countries mainly "industrial"—it is no easy matter to form a mental picture of the profundity of the change, and the magnitude of the consequences, chiefly due to the adoption of a currency in some form. Neither is it easy to frame some formula of words which would constitute a sufficiently accurate generalisation of the nature and essence of the change. The nearest expression of it would appear to consist in this: that it enables men to capitalise their services and the products of their labour into claims on the services and products of posterity. As a consequence, a new direction is given to the mental development of the race, which, in its turn, is the cause of the evolution of a higher physical capacity in the production of wealth. We shall be better able to follow this by presenting it in a few illustrations of the operation of the economic process.

In many villages in Russia, for example, a considerable proportion of the work needed to serve some common purpose is performed (or used to be until comparatively recently) collectively. Thus, it having been decided to build or repair a road between two villages, the elders of the villages make a call on all the able-bodied men to give so much labour, in regular rotation, to the work of construction. The same method is adopted sometimes in building a ferry or a floating-bridge, or in damming the banks of the river. No money passes. The villagers build the road, and then have the use of it in common. The result of this accumulation of "capital" is, as we know, an increase in future production. Let us suppose, then, that each villager is called upon to give six hours in the

course of the week to the work of road or bridge construction. These six hours of work are, in effect, his savings. He has produced more than he has consumed ; and though in this case he gets no general claim representing the value of the labour given, he has a common right in the use of the road or bridge. The six hours' work per week may be a case either of producing more than he did before or of consuming less than he did before. If the hour per day which he gives to the road-making is in addition to his customary hours of work, then he is in a position to consume as much as he used to, but only at the cost of extra labour in producing more. If that hour is deducted from the time usually given to other work, then he must be obviously satisfied to consume less than he did before. In either case he is producing more than he is consuming, and is saving some of the product for future consumption—in this case, the use of the road or bridge.

But even where the work has become more or less specialised, requiring both some amount of expert knowledge and trained physical aptitude, there are still means of doing it without the use of money, which is adopted on occasion. Thus, the road making may be put in the hands of trained navvies, but instead of paying them in money they are "bilked" in daily or weekly rotation amongst the villagers, who provide them with food and lodgings. The modification in the actual process is of considerable importance to our intellectual conception of saving, though essentially the same in effect. The "saving" is still effected by self-denial, either in producing more than before or in consuming less than before ; but the actual "capital" saved is produced by proxy, the act of saving consisting in abstaining from consuming a part of one's product, thus leaving a "surplus" to be

consumed by the road makers. The road makers must have food, clothing, and shelter—to say nothing of tools, the result of previous saving—and unless that is produced by others and handed to them for consumption, the road could not have come into existence.

Let us now take another stage in the collective production of work of public utility. Instead of the road or bridge builders being paid in kind, the municipal authority now levies a money tax on the citizens, out of which the bridge builders are paid wages. The economic process now gets covered up in a wrapper which hides its nature, making the uninitiated gape with wonder at the marvellous power of money ; but actually the process is exactly the same as it was before. A, citizen and bootmaker, is called upon to pay a tax. Either by sitting longer over his last or by spending less on his household, there is a pair of boots remaining as "surplus." He takes it to B, the retail trader, and gets for it a string of shells—perhaps, for convenience, we had better say ten shillings—which he pays over to the tax-gatherer, with many silent imprecations. The ten shillings goes in wages to one of the men employed on the bridge, who presently spends it in buying a pair of boots. C the farmer, D the tailor, and all the rest of the industrious citizens, equally abstain from consuming some part of their respective products, the money for which the things are sold being paid in taxes. That money, paid in wages, is brought back by the bridge builders, in exchange for the things produced by the citizens ; and being once more in the hands of the dealers, is now again ready to perform the function of the tool for transferring the products of the citizens to be consumed by the bridge builders. The compulsory nature of such a saving process may make a difference in the mental condition which leads to saving generally, in proportion

as it leaves a rankling sense of injustice or arbitrariness ; and particularly if it engenders a fear that one's savings may be subject to virtual confiscation, under the guise of being taxed, at the mercy of an autocracy or other oppressive form of government. But in so far as the process is carried out, the bridge comes into being by the fact that the citizens are producing more than they are consuming ; just as was the case when the actual construction was done collectively, or when the builders were paid in kind instead of in money.

But the actual physical process is in no way altered if, instead of being undertaken by the municipal authority, the bridge or road is built by "private enterprise," with the object of securing an income in the future, by charging toll to the users. For the moment we are not concerned with the particular means by which the savings now being applied to building the bridge have been accumulated. Let us suppose that they were amassed by the industry of weaving cloth, or tanning hides. For a number of years the cloth-maker has been producing a "surplus," which he let others consume, receiving in exchange whatever happens to be the currency of the country, constituting a claim on the production of others, which he put by for future use. He then decides to use his savings, not on things for immediate consumption, but in the construction of something—*e.g.*, a bridge—which is to be an instrument to facilitate further production ; calculating that the users of the bridge—those whose product is increased by the employment of the tool which he has provided—will be willing to give a certain share of that increase for the use of the tool ; a share such as the economic conditions enable him to command. That he expresses his income in terms of profit or interest does not alter the fact that he shares in the increased product resulting from the use of the more efficient instrument of production.

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How, then, does the bridge get built ? You cannot put down a heap of money on the river bank and find a bridge evolving from it in course of time. Men must labour to produce the bridge ; and these men can only give their labour by the fact that a number of other men are in the meantime providing them with the things necessary for their maintenance. Once more, then, it is the citizens within the "circle" who produce from day to day the things necessary for the maintenance of the bridge builders ; and once more, the fact that such a provision is made means that they are consuming less than they are producing, thus leaving a surplus to be consumed by others. Were they not doing this—if they were consuming all they produced, or were unable to produce more than is only just necessary to keep them alive—then no bridge would be built. We get here back to the bed-rock principle that the fact that something is being produced which is not an immediate means of supporting life means that, between them, the "circle" is capable of producing a "surplus" of necessities, thus setting free a quantity of human effort to be applied to the production of things other than necessities. The greater the quantity of effort diverted to the production of comforts, luxuries, tools, implements, machinery, and other capital, the greater must be assumed to be the stream of necessities poured out by those whose labour is given to their production. That the cloth maker has come by his claims as a just return for having given the results of his labour to be consumed by others will not avail him in the least for detaching labour from the production of the things needed to sustain life and set them to building a bridge, unless those so detached can be maintained by a surplus of necessities produced by others practically from day to day.

The economic importance of saving must, therefore, be

realised to consist, not at all in the fact that money has been saved, but that in the act of saving a vast stream of utilities is created which, without the desire or necessity to save, would have had no existence ; and that the wider and keener the desire becomes, the greater the volume of that stream, since there is no means of saving otherwise than by producing a surplus. This is not the same thing as saying that whoever produces a surplus (*i.e.*, consumes less than he has produced) must necessarily be in possession of savings—a matter which we shall develop later ; but it is true that all savings represent a produced surplus, whether produced by the "saver" himself, or by proxy. We are not supposing, of course, that before the invention of a currency the desire to save was wholly absent ; but that the new mental outlook developed as a result of an instrument which commands utilities at sight, coupled with the increase and diversity in production due to division and specialisation made possible by use of an efficient medium of exchange, serving as it does to whet the appetite to possess, the incentive to save grows progressively keener, thus spurring men to greater industry, and with that to greater physical aptitude and capacity to produce wealth. *Pari passu* with that increase, and consequent on the progressively available surplus, human effort is set free for the production of more efficient tools, implements, and other instruments which make production still more prolific. Men of higher mental capacity, and perhaps a larger share of ambition, are enabled to think out new methods of organisation and co-operation which still further add to productive efficiency. All these, in turn, provide an additional surplus for further detachment of labour to the production of things of higher and more permanent value ; for work of public utility ; for subsidising learning, science and research ; for the cultivation

of art in various forms ; in short, for the attainments of a higher civilisation. One gets a truer grasp of the economic problem in proportion as one realises how big a slice of it is really a problem in psychology.

Before proceeding to our next point, something must be said on the meaning of the term "surplus." In its ordinary acceptation, it means something left over, that which is more than is really wanted, at any rate for the immediate purpose in hand. Used in this sense, without some qualifying term or mental reservation, it is clearly not applicable to wealth in general. Whatever may be the case with an individual millionaire, the world is not troubled with a surplus of wealth, in the sense that there is more than enough for everyone who cares to have. Yet the term "surplus wealth" is in familiar use in economics ; and I am aware of no other expression that will more concisely present the conception for which it is made to stand. It means that part of created wealth which is not consumed by the producer thereof, individual or nation. Thus, if A—farmer, tailor, engineer, or what not—creates 100 units of produce, but only consumes 70 units, then the 30 units which he does not consume is "surplus wealth." If the United Kingdom as a whole produces, say, eighteen hundred million units of product, but only consumes sixteen hundred millions, then the two hundred million units not consumed is the national "surplus wealth." Whether the individual "saves" the 30 units himself, or it is taken from him as rent, interest, and so on, that part of the wealth which he has produced but does not consume (or the equivalent for which it exchanges) is the surplus wealth created by him. Whether the nation invests its savings abroad, or materialises it into fixed capital at home, that part of the product which is created but not consumed is

the nation's "surplus wealth." It is not assumed that in the extremely complex co-operation of modern industry, we have the means of measuring, even with the remotest approximation to accuracy, each man's productive capacity or efficiency. But though we have not the means for measuring, each worker's product must be some definite quantity in the total of utilities created. With the reservation, then, that it does not mean an overflow—something more than is wanted—the term "surplus wealth" represents a clear enough conception.

Of the wealth created by a producer, part of it he may consume himself, while the rest he will exchange for other utilities, which he may also consume, thus leaving no surplus. Farmer A may be consuming part of the products which he grows, while the rest he will send to market. England produces a large quantity of cotton goods, part of which is consumed at home, and the rest is exported abroad, to be exchanged for things produced by other nations, all of which may be consumed. Though there is no "surplus wealth" in these cases, yet it is highly convenient to find some term which will differentiate that part which is consumed by the actual producer thereof, individual or nation, from that part which is exchanged for other utilities, whether at home or abroad. By tacking on the word "product" to "surplus", we get a term which tolerably well represents the difference. "Surplus product" will then mean that part which a producer exchanges for other things and services, though there may be no "surplus wealth." The farmer exchanges his surplus wheat, and England exchanges its surplus of cotton goods. Indeed, each producer lays himself out for creating "surplus product" of the particular utility upon which he is engaged, so that he may exchange that surplus for other utilities. Indeed, the whole of what he produces may be "surplus

product." But there is no "surplus wealth" unless the total amount consumed is less than what has been produced.

"Surplus wealth" and "saving" would thus appear to be one and the same thing, since there can be no saving otherwise than by producing surplus wealth; yet it would be erroneous to think of them as convertible terms. If Smith has saved, it certainly follows that surplus wealth has been produced; but it by no means follows that he was the actual producer thereof. He may have received it in the form of rent, or royalties, without having produced anything; yet it would still be correct to say that he had himself saved, since he could, of course, have consumed the whole of his receipts, instead of which he preferred to abstain in order to save. Or if Jones has produced surplus wealth, it by no means follows that he is himself the owner of "savings," since the surplus wealth may have been appropriated by Smith aforesaid. Nor yet does it follow from the mere fact that surplus wealth has been produced that any saving at all, either personal or real, has been effected, since those entitled to the surplus wealth may have consumed it in luxuries. It would, therefore, be entirely erroneous to assume that one who has saved must of necessity be the actual producer of surplus wealth; or that a producer of surplus wealth must of necessity have saved; or, indeed, that the production of surplus wealth, in the individual sense, means of necessity any saving at all. A national surplus, looked at from the strictly national standpoint, must constitute saving; but the surplus wealth created by an individual does not necessarily represent any saving at all. We shall see this even more clearly, I trust, at a later stage of our investigation.

One more probable misconception must be removed, and then we can proceed. The changes which have been

delineated as due largely to the invention of a currency must not be understood as depicting economic advance in a straight line. No human progress proceeds in a straight line; the retarding and reactionary forces are, unfortunately, too strong to be overcome without a struggle; it is more like a temperature chart that one sees in a hospital over the bed of a patient recovering from fever. For one thing, the currency itself had to pass through many vicissitudes on its way to fitness for survival. With each breakdown of the system there was a tremendous reaction, from which recovery was slow. Then the system of slavery retarded much of the possible advance; and at all times there have been retarding forces at work in the economic structure. There were also many long periods of stagnation, due to wars and various other causes.

Perhaps a few words may be said to avoid one other possible misconception. The reader must not carry away the impression that it is intended to convey that economic advance is necessarily on all fours with social advance. By economic advance one means increased efficiency in the production of wealth. But that the capacity to produce more wealth means in all cases greater and more widely distributed happiness does not by any means necessarily follow. It is the business of the economist to study the conditions which conduce to wealth production; it is the business of the student of ethics to study the conditions whereby the increased wealth may conduce to an increase in social welfare.

CHAPTER IX

LAND OWNERSHIP—ITS JUSTIFICATION—RENT—MONOPOLY NATURE OF PROPERTY IN LAND—WEALTH—CAPITAL—FACTORS OF PRODUCTION—LAW OF WAGES

CHANGES in the social and political structure of a nation depend in a large measure upon an increase of wealth; and these changes, in turn, alter and modify the economic structure. Only among pastoral peoples is all land held in common. With the development of agriculture, with the increase in wealth and the capacity to produce wealth, the arable and urban land of a country becomes parcelled out into exclusive occupation—sometimes, as in the feudal period, under tenure from the King, and at others into private ownership—leaving only some "common fields" and pasture tracts in communal ownership, *e.g.*, the village "commons" in this country. While the owner is also the tiller, the tendency is for division into holdings no bigger than is capable of being worked by the owner and his family; but when, later, man discovers that land can command rent—coupled, of course, with State protection of proprietorship—the tendency sets in to ownership of large estates, which only special legislation—as, *e.g.*, in modern France—may arrest to a greater or less extent. With the history of social and political development we, as students of economics, are concerned only in so far as those changes affect the economic structure and mechanism.

Thus, we are not concerned with those stages in social evolution when land was worked by slave and other forms of compulsory labour, which is now a thing of the past in practically all civilised countries.

Rent, as we already know, is the measure of the "restriction of access" to superior producing capacity. One piece of land may be superior to another (1) in natural fertility, (2) in ready access to water for purposes of irrigation and household use (3) in being part of an urban site, in demand for building purposes, (4) in being near a populous town or district, thus having a market ready at hand, (5) in being near a railway (6) or waterway (7) or good road, thus reducing the cost of transport, (8) in containing mineral substances which are in demand, (9) and even the mere beauty of position and surroundings must be counted as superior producing capacity, though the additional product consists only of the satisfaction of a mental desire for picturesque landscape, or view of river, sea, forest or mountain. If, then, a piece of land owned by A can yield a 100 units of product for a given effort, while another piece owned by B will yield only 60 units for the same effort, A has 40 more units of income than B, as the result purely of exclusive access. In the case, for example, of land in the City of London, it is no exaggeration to say that the productive capacity of a piece of land—by which is meant its actual capacity to produce wealth, not merely what we know as rental value—may be many thousand times greater than the capacity of another piece of the same size in some rural district.

But, in course of time, man discovers that he can draw income from the ownership of land without the necessity of expending any effort worth mentioning. Thus B, who has access only to land which will yield no more than 60 units for a given effort, is found willing to work

A's land and give him, say, 30 units of product as rent, as by this means he secures for himself 10 more units than he could have got by working the only land to which he has access. A would, naturally, not be satisfied with an income of 30 units as against B's 70 units; but if, instead of owning no more than one piece of land, he can secure six, or sixty, pieces of similar quality, either by favour of the King, or by "Acts of Enclosure" passed by Parliaments, or by purchase, then he can secure a more or less large income from rent, without the need of engaging in any work of production. With the purely economic advantage of the ownership of large estates, there comes to be associated a certain social prestige and stamp of nobility, coupled with a natural human instinct—not entirely devoid of ethical merit—to play Providence to a host of dependents, ready to yield servile homage to their "superiors." Thus the ownership of large estates frequently amounts to a passion in which the economic consideration plays quite a secondary part. There are owners of agricultural land whose incomes are smaller than they could secure by selling the land and investing the proceeds in securities at interest, or by engaging in business. Many a noble landlord will rack-rent his town property, while dealing liberally with his agricultural tenants, and distributing a considerable part of his income from that source in doles.

The rent of land would, therefore, appear to be of quite a different nature from the rent accruing through exclusive ability or other economic advantage. Thus, even if we take such a complete case of exclusion as the ownership of patents, or of copyright, something that has been produced is being given up to be consumed, some concrete service is being rendered, if not by the actual owner of the patent or copyright, at any rate by someone; whereas

land is purely a gift of nature, and the owner, *qua* receiver of rent, gives no service whatever, but only his permission for someone else to produce. Now, it would be a most serious blunder to assume that the ownership of land has not, and never had, either an ethical or economic justification, for the reason that land is not produced by man. Only within recent years we have seen, in America and elsewhere, that where fertile land which can be brought into cultivation without much difficulty can be had practically for the asking, it is not used to the best economic advantage. Instead of "nursing" the land, by methods well known to agriculturists, the settler would work it dry to its last possible capacity, knowing that when it became exhausted he could move on to a fresh patch. Generally, however, the clearing, draining, fencing, and other work requisite to bring virgin soil into a state of cultivation involves prolonged and exhausting labour, to say nothing of having to "rough it," and the need of securing food from other sources pending the time when the land will begin to yield a sufficiency. It may safely be assumed that the conditions were much more onerous in the past, if for no other reasons, because both tools and means of transport were of a more primitive and inefficient type.

It stands to reason, then, that without security of possession, land would not have been brought under cultivation, and man must have remained in the pastoral state. That some of us have different ideas to-day of how public ownership can be made consistent with the fixity of tenure which—we may allow at least tentatively—is needed to secure the best economic results is beside the point. You must first catch your hare before you can cook it. The soil was made fertile as a result of the recognition of ownership; and since it is the fertility that matters, then man has "produced" land in the economic sense—*i.e.*,

he has, within certain limits, created its wealth-yielding capacity, as a consequence of the condition of ownership. As related, however, both to the facts and the results of land ownership as they exist to-day, ethical considerations crowd upon one in great profusion, which, important as are the issues to which they relate, are, nevertheless, of little more than academic interest. He must be, indeed, a sanguine land reformer who imagines that society will incontinently go back on its past, and dispossess without compensation all landowners who cannot show a clean title to having "produced" land in the economic sense. We shall get much more effectively at what is, after all, the true ethical bearing by an investigation of the purely economic aspect of the question, since the two happen to be, at bottom, really identical.

To do this we must now hark back for a short space to our owners of copyrights and patents. Now, from the ethical standpoint, the right to exclusive ownership in the creation of one's intellect would seem to be undeniable. Yet, as an actual fact, society either does not admit that right at all, or if it does, it makes it subservient to the general advantage, since it grants protection for only a limited number of years, obviously as a mere inducement to the exercise of the artistic and inventive faculties, not as an "inherent right"—whatever that term may mean. The evident principle underlying this attitude is, that society will not consent to recognise proprietary rights where such a consent would result in monopoly, however perfect in theory the ethical claim to the right may be. The argument is, that where a man is accumulating concrete wealth, however great in quantity, he is, theoretically at least, not preventing others from doing the same. Since the recognition of property in one's product is not alone an economic advantage, but is the very essence of

economic development—since no one would produce anything beyond his immediate needs if he were liable to be robbed of it at any moment by someone stronger than himself—society agrees to afford each other protection in their possessions, taking, perhaps, the evil of its extreme application as inevitable to securing the economic good that is in it. But to protect each other from being despoiled of concrete possessions is quite another matter from affording protection against the infringement of ideas, thus creating a monopoly, which is not an economic good. It is one thing to say, "This thing is mine," but quite another to say, "No one shall be allowed to make another like it without my permission." In effect, Society says: "A fig for your ethical theories: we are only concerned with mutuality. We will protect you only to the extent that we, in turn, want and expect your protection; but not where your protection means the exclusion of all others. To secure a general advantage, we are willing to give you something that will be just sufficient inducement to the best exercise of your faculties, but no more than that." Whatever the fine-spun theories of Ethical Sanction, or Categorical Tests, Mutuality is in the end the ultimate Ethical Standard.

If we apply this principle to the ownership of land, we have all that is needed to guide us to the economic issue, and, incidentally, the ethical issue is bound up with it. Even in new countries, where large tracts of land remain available for occupation, tillage, and pasture, land is still in the nature of a monopoly. It is no use telling the merchant or banker in London that he can have as much land as he cares to occupy in Little Slocum at a rental of a few shillings, or the tailor in Quebec that thousands of acres are going begging in the West. It is even of little use telling the farm-hand in Somerset that there is plenty

of land in Australia or Argentina. In old and thickly populated countries, the entire soil is the monopoly possession of the few—in some countries more so than in others. You cannot duplicate a piece of land as you can a coat, a pair of boots, or even a Marconi apparatus. It is idle to point to land elsewhere when only land in a particular location can be put to the desired economic purpose. The question which concerns the economist is not "Is land monopoly ethically right?" but "Is land monopoly conducive to the maximum production of wealth?" True, man has, within limits, "produced" land in the economic sense (we will say nothing here of ownership in mineral wealth, in rivers and lakes, or in what is known as unearned increment); but so am I producing this book in an economic, and most obvious, sense. And yet society denies my children the right to inherit the ownership of it for more than a few years. That, says society, would be to create a monopoly, and all monopolies are a drag on production. In the same way society can decide to make land ownership subservient to the general economic needs—to refuse its protection beyond the limit necessary to foster the incentive to the best economic use of land; or at any rate to impose such conditions as will secure that end.

This view of the matter, however, by no means covers the whole case. As has already been enforced elsewhere, the economic structure is not built up of a definite quantity of dynamic force, in which the human units are so many cogs, levers, and pulleys. The mental condition of mankind is, when all is weighed, the greatest factor in the complicated mechanism; and mental condition is by no means necessarily the same as reasoned conclusion. Now, security of possession is the great regulator which keeps the mental balance in economic working order. Where

the security of property is small and uncertain, production languishes, and nations remain poor. It matters little that the particular kind of property which is attacked happens to be without economic or ethical justification, or both. The bulk of mankind are not capable of analysing or understanding such nice points. They only see the things which are plainly obvious and on the surface. As it happens, property in the creations of one's intellect was at first not recognised at all ; and it was only very late in the history of social evolution that a measure of protection was decided to be desirable. Thus, men have become accustomed to look upon that as a mere concession, many still deeming it to be an unnecessary and unjust concession. But property in land has grown up from the very cradle of the race owing to its being, under the conditions in which it grew up, an indispensable factor to economic evolution. The exceedingly delicate and complicated mechanism of modern production, built up on a vast system of credits, is based on a recognition of ownership ; and any violent disturbance of property in land, though intended to leave the credit claims in full force, would disorganise the mechanism in a disastrous fashion, by throwing the mental balance out of equilibrium ; when the attempted remedy would probably prove infinitely worse than the disease which it set out to cure. To put the matter in another way, social and economic evolution can proceed no faster than the mental factor is capable of being attuned to the new conception and outlook ; and this can only come by slow degrees—just in proportion to the educational forces which are brought into play to recast the intellectual fibre. When later we come to review the economic structure as a whole, we shall have something further to say on the question of property in land.

But side by side with the gradual absorption of the land

of a country into private ownership, there also grows up accumulations of capital, the meaning and effect of which we must now proceed to investigate. We shall then be in a position to summarise the vastly important changes in the economic structure and mechanism due to these two great facts ; and to see in what respect these changes modify our hitherto conception of the laws governing production, and the resulting incomes accruing to the various agents engaged in production.

The term "wealth" has already been defined incidentally, and little more will be needed to amplify it. All things and services which men desire to have constitute wealth. So far as concerns the meaning of the term "wealth," no distinction can be drawn between necessities and luxuries. Both are wealth, though one kind of it may be more desirable than another—a matter which will receive further consideration at a later stage. With three important qualifications—one of which has already been dealt with—our conception of wealth will cover all that concerns us as students of economics. The wealth which the economist is in a position to deal with must have the quality of exchangeability—it must be some thing or service for which others are willing to give something else in exchange—in the parlance of the market, we should say it must have a price. It is further necessary to draw a clear distinction between actual wealth in existence and latent or potential wealth. At the time of listening to music I am the recipient of wealth for which I am paying a price ; but the capacity to render the music is not concrete wealth, but potential wealth. Both individually and collectively, potential wealth is real in the economic sense, in so far as it can command utilities in exchange. Conceivably, a particular nation may be exceptionally gifted in musical talent,

while next to incapable in all else, and yet may be able to draw a handsome income in general utilities in exchange for providing other nations with musical talent and compositions for which they are willing to pay. A nation of people well skilled and trained in various industries will have a quantity of potential wealth, in addition to whatever concrete wealth it may be in possession of at a given time. A country may also have potential wealth in the fertility of its soil, the mineral wealth which the soil contains, and even in favourable climatic conditions and developed habits of steady application. It matters little, however, what term is employed to express a conception of the facts, so long as the conception is clear-cut and accurate.

The third qualification is, that we must draw a clear distinction between individual wealth and national wealth. Since wealth has for its object the satisfaction of desires—without that quality it cannot conceivably be wealth—it follows that personal claims on others which entitle one to receive from them things and services for the satisfaction of one's desires constitute one's wealth. But the very smallest consideration will show that such claims cannot constitute national wealth—unless they are claims of one nation on another nation. Thus B and C are each indebted to A for £100—in effect they have to render goods and services to that value for the consumption of A. If A's actual possessions are valued at £1,000, then his total wealth is equal to £1,200. But supposing the possessions of B and C are also valued at £1,000 each, their combined wealth is not £3,200, but only £3,000. The student will do well to keep this well in view, obvious as the proposition is. At a later stage we shall have to amplify this consideration in reference to the possession of money. For the present we have all that we need to know of the conception of wealth.

But things may be desired objects of possession as ends in themselves—for direct consumption—or as means to ends—to be used for producing more wealth. These latter will consist of tools, machinery, buildings in which industry or trade is carried on, harbours, docks, canals, ships, railways, telegraphs, telephones, roads, bridges, and an endless number of other things. Wealth in this form is best expressed by the term "instruments of production." But for a certain reason, with which we shall deal presently, it is more familiarly known as "capital." Capital may, therefore, be defined as that portion of wealth which is used to produce more wealth. While, therefore, the total actual wealth of a country is a fixed quantity at any given time, its capital is a variable quantity. Thus, a building which is one day used as a private residence—as we should say for consumption—may next day be converted into a workshop for producing more wealth, and so become capital. The capital of a nation cannot, therefore, exceed its total wealth (unless it borrows from other nations on the security of its potential wealth), but may be any part of the total wealth. The consideration is of importance, inasmuch as the frugal and industrious nation—like the frugal individual—may employ a greater proportion of its wealth as capital than the extravagant and improvident nation, which may prefer to go on consuming its wealth. The reader should bear in mind that for the present we are using the term "capital" to mean only actual instruments of production.

As man advances in the arts of producing wealth, he becomes progressively more dependent on efficient instruments of production. But with the private ownership of the more fertile land, which leaves many with a reduced income, as a result of the restriction of access; with exclusive access to industries and professions owing to ability

more or less rare ; with varying dispositions to save : the wealth usable as capital accumulates in the hands of the few. At the same time, the arbitrary power of kings, and social and political forces of various kinds, tend to entrench a privileged class in their possessions, and to prevent dispersal. Gradually a section of each nation gets completely squeezed out of access to any natural resources whatever. The members of the nation become sorted out into sundry economic divisions, which may be enumerated as follows : (1) Those who derive incomes from rent of land ; (2) those who, owning both land and capital, themselves engage in production, and derive an enhanced income in which is included rent and interest ; (3) those who, having no land, carry on industries with their own capital, and after paying rent derive an enhanced income (as compared with those who are without, or with less efficient, capital) in proportion to the scarcity of capital, and the more or less exclusive nature (if any) of their occupations ; (4) those who (at a later stage) derive an income from lending the use of capital ; and (5) those who have neither land nor capital, and who can, therefore, only secure an income by indirectly paying for the use of capital (in addition to rent) by sharing their product with the provider of the capital necessary to the industry.

We then get what is known in economics as the four factors of production—land, capital, labour, and organising ability. All the four factors can be combined in one person. But where they are not so combined, the three factors first named cannot produce otherwise than in co-operation with each other. Land cannot be worked without tools, farm buildings, and so on, and the tools must be wielded, guided, or supervised by human hands and brains. If the production is what we know as industrial, or is part of the work of distributing, the factory, shop, or

office must stand on land, and men must labour to produce. The fourth factor—organising ability—is generally combined with capital in the person owning the capital ; but as understood in the sense of exceptional ability, it is not an indispensable factor in production. More efficient organisation—in effect, more accurate adjustment of co-operation—will result in greater production ; but certain routine adjustments in most industries become more or less stereotyped, requiring no ability beyond ordinary experience.

It is idle to apply the criterion of accessibility to one who has no access to any income-yielding source whatever—often not even in the possession of a few simple tools, or the training requisite to the minimum of productive efficiency. The income of that section which has neither land, capital, nor special ability must obviously depend upon some other law than Freedom of Access—by which is meant that the income of a person cannot, in the long run, fall below the minimum which he is capable of obtaining from another occupation freely open to him. The worker's income is now received in the form of "wages," but, at bottom, it means a certain stipulated share of the utilities produced by the three factors working in co-operation.

Now, since neither land nor capital can produce anything except with the co-operation of labour, it would seem at first glance that labour is in as good a position to bargain for its share as are the other two factors. But this depends upon the quantity of labour seeking to be employed in relation to the quantity of employment on offer at a given time. If the quantity of labour exceeds the employment offered, the workers will be bidding against each other to secure the employment. It does not follow as a matter of course that with a proportionate increase in the ranks of

labour, as a consequence of the accumulation of land and capital in fewer hands, the disproportion between employment on offer and labour-seeking employment is correspondingly increased. Employment—in other words, the production of wealth—is not a fixed quantity. Manifestly, the two primary facts controlling production are (1) Nature's capacity to yield in return for human labour, and (2) the quantity and efficiency of the "instruments of production" in existence at a given time. The subsidiary fact—but of little less importance under modern conditions than the primary facts—is man's capacity to organise the most effective measure of co-operation in the various industrial units, and the co-ordination of the functions of the many units to a common end. This is the problem which man has been blindly groping to solve for untold ages, and which economics sets itself to elucidate with scientific certainty of principle, if not with quantitative precision. But as it is, it is only on very rare occasions in history—as after the great plague in this country—that labour did not exceed the quantity of employment available. What, then, is the law which governs wages?

This is generally stated as the law that "wages cannot fall below the minimum of subsistence." In so far as it is true, it resolves itself on final analysis into the very obvious physical law "that the man who is dead cannot work." When one attempts to put the law into the form of a logical demonstration, it comes out something after this fashion: Since life can only be perpetuated by producing the means of sustaining life, and since labour is a necessary part of production, it follows from the fact that life is perpetuated that labour must have subsistence, else it would not be there to produce. Now, if by subsistence we are to understand healthy subsistence and the ability to rear a family in healthy working efficiency, and that no

worker can be paid less than that, then the proposition is obviously and glaringly untrue. On the one side of the scale the skilled worker will get more than bare subsistence, owing to relative scarcity; particularly when the scarcity is artificially enhanced by trade-union combination. On the other side of the scale, many thousands are paid a wage below the level of healthy subsistence, and some of them do, as a matter of fact, die of starvation more or less slow, and leave no healthy children to stock the "labour market." That from the fact that a man keeps at work one is bound to assume that he has meals and a bed of some sort, though, for all we know, he may be on the road to breaking down, may readily be granted for what it is worth. The fallacy of the syllogism is that certain terms are left out both from the minor premiss and the conclusion. "Some" labour is necessary to produce just that quantity that is being produced—varying, nevertheless, with the quantity of labour-saving appliances; and what follows is that, to the extent that life is being perpetuated—not necessarily to the extent possible with a more efficient organisation of production—"some" labour must have subsistence sufficient to enable them to procreate in numbers that will keep up that quantity of production, else the quantity would be less, and life could not be preserved to the extent that it is. The proportion that go under do not count so long as there are enough left to keep the labour market stocked to the extent of the actual demand. This is what remains of the "law" when reduced to its exact logical value; and there is no need to pursue it further.

The facts of the case are rather different from a law of wages based on the minimum of subsistence. From the economic standpoint employers are discovering that starved labour is generally inefficient labour; and this not

alone, or even mainly, from the physical standpoint, but from the mental standpoint. Production under modern conditions is to an enormous extent a matter of mental capacity, on the part of the worker as well as on the part of the employer. Just as figs will not grow on thistles, mental capacity will not flourish except under conditions of tolerable economic ease. In the second place, only occasionally have wages been subject to pure economic law or tendency. When, as in the earlier part of last century, wages in factories were wholly regulated by economic pressure, the consequences were deplorable in the extreme. In many trades they have been so until very recently, and in some they remain so to the present day. But in many, if not most cases, other forces modify to a greater or less extent the mere economic tendency. In some respects, workers had an advantage in the past, public opinion being more closely in touch with the workers, and employers being, therefore, more sensitive to the moral and religious influence of their environment. If incomes were smaller as a whole, no one was left to starve. In other respects, what with trade unions, direct State action, and the constantly increasing political influence of the masses in this country, wages to-day (particularly if we include *conditions* under which labour is carried on) is certainly not a mere question of economic law.

As applied, then, to the factor of labour, our conception of the law of Freedom of Access must now be considerably modified. The minimum of income in any occupation depends, as we have seen, upon the amount of income that one could derive, in the final resort, from some other occupation to which one has perfect freedom of access, both in the sense of the natural resources being at his disposal, and his ability to fashion those resources into utilities. But when labour becomes entirely divorced

from either land or capital, the access to natural resources is quite absent (even sea-fishing requires some capital); hence there is really no economic limit to the minimum income of unskilled labour. In the case of skilled labour, the law partially operates—*i.e.*, though excluded from access to land and capital, his access to superior skill will secure him the advantage, as compared with unskilled labour, of both more frequent employment and higher remuneration, resulting in a bigger income in the long run.

But “instruments of production” is not the only “capital” requisite to production. Pending the fashioning into “goods” of the natural materials that are in the course of being worked up, the factors engaging in the production must all be fed, clothed, housed, and in many other respects provided for, in a relatively small part out of utilities already in existence, but as to the major part out of utilities produced from day to day—nay, from moment to moment—by all those engaged in production in every part of the world. In addition, then, to the “materials” and “stock” requisite to carry on production—the buildings, tools, machinery, raw materials, and various other things necessary to set an industry in motion—the organiser of the industry must also be able to command the means for the maintenance of himself and the workers engaged in it pending the time when the particular process of production upon which they are engaged results in the emergence of completed “goods” ready to be placed on the market, and so command other utilities in exchange. In so far as that maintenance is drawn from existing sources, the capitalist-organiser may, conceivably, have himself accumulated a supply for the purpose. But in so far as that supply must be drawn from a stock in the possession of others, and most of all from a stock emerging

into being from day to day, he must be in possession to that extent of claims on production, accumulated as a result of past saving.

I can fancy someone opening this book for the first time just at the preceding paragraph, and, after reading it through, exclaiming in disgust: "What a stupidly round-about way of stating the simple fact that money is required to carry on industry!" But the reader who has read from the beginning will, I am fain to believe, fully realise the necessity of escaping the utterly distorted conception of the economic process which a statement in unqualified terms of money almost inevitably engenders. As we shall see very shortly, if by money we are to understand "coin," then it is very little of that indeed that helps to carry on industry. We are far nearer the mark in saying that, in addition to actual implements and stock, a certain quantity of "claims" on the production of others is necessary, than by saying that it requires a sum of money. We must now proceed to develop the mechanism of industry as carried on under modern conditions, having now, as I trust, fully prepared ourselves to follow it accurately, without confusion of thought.

CHAPTER X

PRESENT ECONOMIC CIRCLE—MINUTE SUBDIVISION—THE STREAM AND ITS TRIBUTARIES—BANKING FIGURES—WHAT THE BANKS ARE LENDING—BANK CLEARINGS—HOW WE PAY FOR IMPORTS—PAPER CURRENCY—GOLD CURRENCY IMPOSSIBLE

THE most vitally important development of modern production consists in the fact that practically the whole world has now become one producing unit. No further than a few centuries back, tradings between nations was practically confined to a few luxuries. For the staple needs of life, each country, each district, was self-dependent. If the crops failed, there was famine, which no money could cure. With the age of steam, and consequent development of rapid communication between countries and continents; with the age of machinery and consequent rapid development of producing capacity, production has become vastly more specialised, and nations have come to be dependent upon each other, not alone for the comforts and graces of life, but for the very necessities of existence—the circumference of the economic "circle of producer-consumers" has widened out to embrace within it the whole of the civilised globe.

More recently still, the levers which set the mechanism of production in motion throughout the world have become completely internationalised, and as completely controlled from a few important centres. What is known as

"Finance" has become during the last half-century the driving force of the whole machinery of production to an extent not even remotely approached in the course of the previous history of industrial development. I doubt not, the man in the street understands by the term "finance" the possession of the necessary coin to start an industry and to keep it going. Not only is such a conception a sheer delusion, but even if conceived as consisting in the possession by those who set the industries in motion of the necessary claims or credits, it is scarcely less complete a delusion. Industries of all kinds are set going and kept in being by means of claims on production in general; but it does not in the least follow that those claims are owned by the actual persons who set the industrial mechanism in motion. "Finance" is a pure "manipulation"—a certain organisation, more or less perfect, for gathering the claims held by many individuals into common "pools," thus making them available for being utilised in further production, under the management and control of the "manipulators." And the instrument used in the process of "manipulation" is very largely of a psychological nature. Much of this will probably be, as yet, unintelligible to the reader; but we hope to make it very shortly perfectly clear.

The next characteristic, of scarcely less vital importance, is the minute subdivision of production into distinct processes, each performed by a different set of workers, specially trained to that work. Each man's contribution to the production of any commodity whatever has now become a mere tiny fraction—more infinitesimal in some than in others, but very tiny, nevertheless, even in the most simple product. Most people have read of the number of processes that the manufacture of a pin goes through—some thirty or more, I believe. One will see at a glance, for example, that the man who drove some

rivets or painted some part of one of our modern mighty Leviathans has contributed the tiniest of fractions to the construction of the complete liner. But it will probably occur to very few that in the very rivet driven into the vessel is embodied the labour contribution of, literally, many thousands of workers. The iron ore out of which the rivet was made may have been mined abroad, and brought into this country by road, ship, and rail, either in its "raw" state or after it had been smelted into metal.

Now, just think for a moment. We begin with the miners; then come the workers in the many processes of smelting, converting into steel, shaping and finishing into rivets. There are the carriers of the ore and the metal in the various stages from mine to factory, from one factory to another, from these to the various railways, docks, and finally to the shipbuilding yard. There are the workers at the docks and railways who handle and load the goods; the captains, officers, and sailors who navigate the ships; the engine-drivers, firemen, guards, signalmen, and others who work the transit. Nor can the managing and clerical staffs in the offices of the various concerns be left out of account. But even so, we are only at the beginning of our catalogue. There are the very many thousands who have been employed in the construction of the ships, docks and railways, the buildings, engines and rolling stocks, the tools, cranes and haulage machinery, and the thousand and one other instruments and contrivances used in the many processes of transport. There are the makers of the carts, lorries, and other vehicles used for carrying; the lumbermen who have cut down the timber used in building the vehicles, buildings, and rolling stock; the raftsmen who floated the logs down the river; the workers in the saw mills where the timber was cut into planks and battens. There are the breeders of the horses

and the manufacturers of the lubricants. All these and many others have co-operated in producing the rivet used in the construction of the liner to which our riveter is now contributing his tiny share. And with all this, we have as yet taken no account of the producers of the food and other necessaries which kept all these workers in the many hundreds of processes in a fit physical and mental condition for the performance of their respective tasks.

We can readily see a close connection, for example, between farming, milling, and baking ; or between tanning, currying and dressing, and bootmaking ; or between spinning, weaving, and tailoring ; but not so readily, *e.g.*, between either of these and mining, iron and steel making, and engineering. We are accustomed to think of these groups of trades, and of many others, as being independent of each other. But a very little thought will show how helpless either of the trades first named would be without the tools and machinery provided by the workers in the mining, metal, and engineering trades ; or how either of these would be impotent without the work of the transport trade—the trade which links together all other trades into one efficient whole. There is, indeed, no such thing as an independent trade. The engineer is just as directly dependent on the leather and weaving trades—in the need for leather and canvas belting—as the latter are dependent on the engineering trades. For the mere purpose of identification and facility of reference when it becomes necessary to deal with details, we may broadly classify trades into the three categories of "extractive," "manufacturing," and "distributing"; but this is not to be understood that they are in any real sense independent of each other, or that any one of them is more essentially a work of production than the others in the economic sense—the only sense that really matters. What we

commonly know as "distributing" trades is more correctly a branch of the transport trade. We do not usually identify the shopkeeper as a transport worker ; we think of him as engaging in profit-making. But in reality he is just as much a transport worker as his porter who takes the parcel to the consumer's door, except only that part of his income is derived from interest on capital, or is enhanced by the degree of scarcity due to aggregation of capital and whatever special ability may be required for organising the measure of co-operation under his control—all of which resolve themselves, nevertheless, into the provision of better transport facilities. The essence, therefore, of wholesale dealing, shopkeeping, and the various operations of Factors, Agents, and a host of other middlemen is the transport facilities it provides by means of convenient centres, finally bringing the commodities within easy reach of the consumers. There are, however, a class of merchant-financiers whose work is essentially a gamble in setting production in motion, which they base on calculations of probable demand ; of which further anon.

Now, if we are to get a real comprehensive grasp of the economic machine as a whole, we must discover some generalising formula which, leaving details to be treated as required, will give us such a true conception of the complete economic structure as is necessary for accurate deduction. We have seen that, under present conditions, none of us contributes more than an infinitesimal fraction to the production of a commodity. The production of this treatise will depend upon the work of many thousands of other workers in the paper-making, composing, printing, engineering, binding, spinning, weaving, and transport trades ; in the inventors of many machines, and the organisation of the publishing trade ; to say nothing of the

many writers on economics for generations past who have taught me what I know of the subject, and the teachers and thinkers who have developed in me what capacity I have for cogent reasoning. None of us gives anything that is actually consumable in exchange for the things which he gets for his own consumption, except the one engaged in the very final process of delivering the commodity at the consumer's door; and he, it may be said, in addition to giving his own labour contribution, is then acting also as agent for all the thousands of other workers whose labour is embodied in the commodity which he is delivering—he is putting, as it were, the final touch to the structure gradually built up by a great host working in a long chain of co-operation. In return for these labour contributions, they become entitled to demand products for their own consumption—demands which they may have exercised long before their own contributions materialise in the finished product available for consumption. In the act of exercising those claims—that is, in the act of becoming consumers—they give up so much of whatever happens to be the instrument by virtue of which their claims are recognised—whether it be in the form of cash, or of credit on a bank, or of what is known as "securities" in various forms—as is equivalent to the value of the products which they take for consumption, a value which contains both the labour embodied in the commodity throughout the many processes through which it had passed on its way to completion, and the demands of the other three factors of land, capital, and ability. The instruments of claim so relinquished by the consumers are then transferred and distributed—in a manner which we shall see presently—amongst the various factors; when the new holders, in their turn, become entitled to demand utilities for their own consumption. But no sooner do they become con-

sumers than the instruments of claim are again relinquished and redistributed in various ways to meet such demands of the several factors as the economic conditions enable them to exact.

We shall get a true grasp of the process if we conceive of products of all kinds as emerging from a vast stream, to which there are many tributaries (Diagram I.). Into these tributaries the workers in the many thousands of processes into which production is divided are constantly contributing; and from these there finally flows into the main stream an enormous volume of finished commodities ready for consumption. The extractive and manufacturing trades will represent the many tributaries, while the retail dealers will represent the main stream which pours out the finished products. In our diagram we have chosen a few important trades to stand as types for the rest. The various trades have connecting channels, indicating their dependence on each other. The arrows in the stream pointing to the right represent the commodities travelling towards the mouth or exit, meaning thereby into the possession of the consumers. The arrows pointing in the contrary direction, and making their way from the stream up the several tributaries, represent the money, or other finance instruments, coming mainly from the consumers, travelling on their way to be distributed amongst the various factors engaged in production, who, by means of these instruments, will become entitled to draw utilities from the mouth of the stream to the extent of the claims which they respectively receive. We shall proceed at once to deal with the operation of the financing process; and a little later we shall get to understand the meaning of the "Derelicts" in our diagram, and the monstrosities with which our stream is dotted here and there.

To those unacquainted with the facts, the following

figures for the year 1906* will be something in the nature of a startler. Subject only to fluctuations quite insignificant as compared with the gigantic totals, those figures are quite normal.

102 Joint Stock and private banks published balance sheets in that year. These show an actual liability (apart from the mere book-keeping liabilities, as subscribed capital and reserve, and not including acceptances) of just on ... £1,000,000,000
In addition to this there was the Bank of England's liability on its average note circulation of ... 28,000,000

£1,028,000,000

Average total coin and bullion, both gold and silver, in the Bank of England,
both departments ... £33,000,000
Coin and bullion in other banks ... 90,000,000

123,000,000

Balance of liabilities over coin and bullion ... £905,000,000

In round figures an excess of liabilities over cash and bullion in hand of nine hundred millions (£900,000,000).

On the credit side we have :—

In loans and discounted bills	...	...	...	...	...	£625,000,000
At call and short notice	...	...	...	...	...	110,000,000
Investments in securities	...	...	...	...	...	255,000,000
Coin and bullion	...	...	...	...	...	123,000,000
Securities in the Issue Department against notes	...	...	...	...	...	18,000,000
Buildings, etc., some	...	...	...	...	...	25,000,000

£1,156,000,000

There are some further small items, given as Sundry Assets. It should be remembered that the loans represent in no sense a possible call on gold, since the borrowers

* The figures are taken from a pamphlet of mine published some years ago. While differing in actual amounts from the figures of more recent years, the relative proportions remain virtually the same.

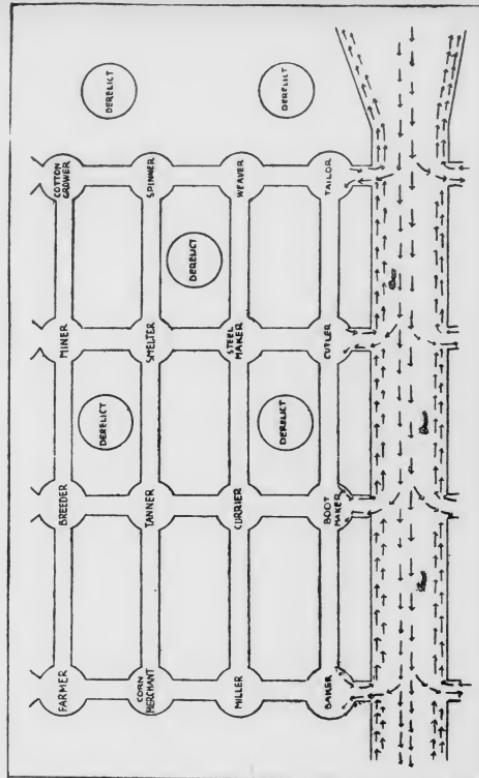


DIAGRAM 1.

keep no gold reserves, their assets consisting of (1) credits on these very banks, (2) general securities, (3) property, trading stock, etc., and (4) to some extent, perhaps, their mere business standing and reputations. There are, in addition, some seventy other British banks, as also a great number of foreign and colonial banks having offices in London, whose proportion of liabilities to coin and bullion may be taken to be the same as the others. These help to swell the enormous total of liabilities exceeding the quantity of gold and bullion in the banks.

Now, in the first place, the reader will at once be puzzled to know what it is that the banks are lending. They make their incomes out of what is called lending money. But what money? Of the £33,000,000 (average) in the Bank of England, a large proportion, depending upon the note circulation at the time, must not be touched, being there as security against the note issue, in accordance with the Bank Act of 1844. If we take the gold and silver in the banking department of the Bank of England (kept separate from what is called the Issue Department), we find that in the ten years from 1894 to 1905 inclusive, the highest amount was £2,393,000, and the lowest £1,658,000—a difference between the maximum and minimum of less than three-quarters of a million. It is safe to assume that the withdrawals of gold from the other banks is not more than the same proportion—if anything it would be less, since any special call on gold is first felt at the Bank of England, where all the other banks keep deposits. Hence, the fluctuations in the stock of gold in the other banks should not be more than thirty millions; but in all probability it is much less than this; I should put it down in normal times as not more than ten millions at the outside. Of recent years, there have been fairly important gold movements between the Bank of England and certain

places abroad—Argentina and Egypt, for example; but these are purely dealings in gold, and have nothing to do with the normal loan market. In no year has the export of gold reached fifty millions; and the import of gold has considerably exceeded the export on the average. It is difficult for one who has been watching the gold shovelled out by the bank cashiers to think of it as a mere nominal amount, and as remaining practically constant in the banks. But one should remember that there is such a thing as a stage army, looming large, but in reality consisting of a small number circling round the wing, front and back. While one customer is drawing gold at one desk, another is paying in gold at the next desk; and frequently the same customer will be drawing gold and paying in at the same time an equal or larger amount, so as to keep records on the paying-in and cheque-books. It is only in the time of money crisis that there is any call on the gold.

If, then, gold in the banks remains practically constant, the question becomes still more insistent, What is it that the banks are lending? Remember, the average amount out on loan in the year named reached the enormous sum of seven hundred and thirty-five millions (£735,000,000), while the actual movements of gold for internal trading was probably not more than ten millions, and could not have been more than one hundred millions if the banks emptied their safes and tills of every penny piece! Well, we shall get some inkling of the meaning of this conundrum when we get to understand the nature of the business transacted by what is known as the Bankers' Clearing Houses. A Bankers' Clearing House is a place where cheques and other credit documents are exchanged one against the other. We shall see this readily by considering a simple contra account between two tradesmen, A and B. A, the tailor, buys his groceries from B on

credit. B from time to time gets suits of clothes for himself and his boys from A. When A receives his monthly or quarterly statement from B, instead of paying the account in money, A balances it "By Contra Account." Should there be some small balance still outstanding, it is carried forward to the next quarter's account, and once more balanced by contra. B similarly balances the accounts he receives from A; and thus they may be buying of each other for years without a penny piece passing between them. What actually takes place is an exchange of groceries for clothes and *vice versa*.

We are now in a position to follow the transactions taking place in the Clearing Houses. A, the ironmaster, banks, let us say, at the London and South Western Bank. In course of trading, he receives a cheque from B, a firm of engineers, drawn on Lloyds' Bank, for £1,000, which he pays in at his bankers—*i.e.*, he instructs them to collect that amount for him from Lloyds. But Lloyds have a customer who paid in a cheque for £1,000 drawn on the London and South Western Bank. Instead of paying each other £1,000 in cash, the representatives of the two banks meet at the Clearing House, exchange one cheque for the other, make entries in books, and, as between them, the transaction is balanced by contra account. But, the reader will say, this is right enough as between the two banks; but A, who has supplied B with goods to the value of £1,000, must get his money sometime or other. A is, however, a buyer as well as a seller. Iron smelting demands the use of a large quantity of coals, and so we may suppose that A has bought coals of C, the mine-owner, to the value of £1,000, for which he pays by cheque. If C should chance to be banking at Lloyds, then Lloyds would have to collect £1,000 from the London and South Western against the cheque drawn by A in favour of C;

while the London and South Western would have to collect £1,000 from Lloyds against the cheque drawn by B in favour of A. Not only, then, will the banks settle their accounts against each other per contra, but A's account at his bankers will also be balanced in the same way. Thus, on the credit side of his account on the bank's ledger there will be an entry of £1,000 in his favour, the amount of the cheque paid him by B; while on the debit side of his account there will be an entry for a similar sum against him, the value of the cheque paid by him to C. In actual fact, A will have exchanged so much pig-iron for coals. B is, of course, also a seller as well as a buyer. He has bought the pig-iron from A for his engineering works; and so we may suppose that he sells to C £1,000 worth of mining machinery. Thus A is indebted to C, C is indebted to B, and B is indebted to A. In the course of bank clearings, the amounts get balanced against each other, and no coin changes hands—there has been merely an exchange of goods.

I had written out some examples of more roundabout clearings; but on reading through what I had written, I came to the conclusion that the reader would soon tire of giving the concentration and the harking-back necessary to follow the identities of the many individuals and banks; while, on the other hand, I think that he may well be trusted with sufficient imagination to mentally visualise the process without more elaborate detail. He will see readily that the cheques subjected to the process of clearing need not be for corresponding amounts; nor is it necessary to cast a balance at every clearance. It is not cheques alone that are subject to clearing, but what are known as bankers' drafts, acceptances, and other credit documents, are equally subject to the same operation. The amounts represented on these documents are entered up at the

time they are handed in, and a balance struck at certain intervals, when any outstanding balance on one side or the other may be either settled by the bank's own cheque, or carried forward to the next account.

We shall better realise the "exchange" nature of business operations when we know the magnitude—the staggering magnitude—of the bank clearings. In the year 1910 the Bankers' Clearing House in this country dealt with the incomprehensible sum of over fifteen thousand millions (£15,403,129,750). We can absolutely form no conception of what a sum like that means. I should like the reader to make a wild guess—a half-dozen guesses, if he likes—of how long it would take to count such a sum, before he reads any further. Let us suppose that one starts counting the sovereigns at the rate of four per second = 240 per minute = 14,400 per hour. We will suppose, further, that he works eight hours per day clear of meal-times, six days per week, all the fifty-two weeks in the year. When he has kept counting for a whole year, he will have got through close upon thirty-six millions. I can fancy the reader thinking: Ah, now we are getting along famously—thirty-six millions is a big sum—we shall soon get through the job. Here he had better stop to take a full breath. If he keeps on counting without a single day's holiday for four hundred and twenty-eight years, he will just have the respectable sum of nineteen and three-quarter millions still left uncounted!

But this by no means represents all the clearings effected. In the first place, business transactions taking place between people banking at various branches of the same bank do not go through the Clearing Houses at all, but are cleared at the head office of each bank. Most of the big banks have branches running into some hundreds. If we take, for example, Lloyds' Bank with its 518 branches and sub-

branches, it will readily be seen that these clearings must represent an enormous sum. Of these, no figures are available. The Stock Exchange has a clearing system inside the House for practically all the principal Stocks, and frequently transactions running in the aggregate into many millions are balanced against each other without the intervention of even a cheque, with only, perhaps, a few shillings to liquidate one way or the other. All the other big Exchanges, such as the Corn Exchange, Wool Exchange, Coal Exchange, and so on, have also similar clearing systems among their members. A certain amount of clearing is also done at the banks over the counters, by means of messengers, or "runners," going from one bank to another. Of all these clearings no figures are available, so that there are no means of estimating the total volume of clearings. What we have to realise is, that this phenomenal sum of clearings represent a corresponding volume of exchanges of goods and services, effected without the medium of a single coin.

It is somewhat curious that many people who are well aware of the fact of bank clearings, and in a general way quite realise that it means an exchange of goods and services without the intervention of coin, are nevertheless under the delusion that our trading with foreign countries—our exports and imports—must be done by buying and selling for gold. This delusion is not quite as prevalent to-day as it was some ten years ago. In the early days of the present protectionist movement (in a treatise on economics it would be idle to accept the political disguise of calling it "tariff-reform"), it was quite common to hear it proclaimed that our excess of imports over exports must mean a draining of our stock of gold. I remember more than one authorised and paid lecturer stoutly maintaining

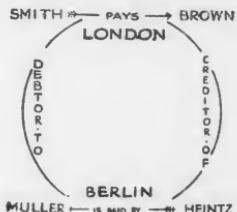
that, spite of alleged figures to prove that our stock of gold is not diminishing—figures, they said, could be made to prove anything: one of the common refuges of the argumentatively bankrupt—there must be some fund of gold out of which the excess is paid. Seeing that our net excess of imports over exports, after deducting re-exports, say for the fifteen years from 1897 to 1911, amount to the gigantic total of close on twelve hundred millions (£1,189,117,006), the proposition is, on the face of it, too puerile to merit serious argument. How the excess is paid for must be left to be explained at a later stage. The propaganda, pro and con, that has been conducted since then has served to enlighten many on this point; at any rate, the contention is rarely, if ever, heard now. Nevertheless, the trading with foreigners otherwise than by buying and selling for gold is still very puzzling to many. They can understand payment by cheque at home, and some can realise what it means; but foreigners, they think, can care little for our cheques, have no access to our Clearing Houses even if paid by cheque, and must, therefore, ultimately be paid in gold for what they sell to us, and that we should want gold for what we sell to them.

In reality, though the method of clearing may be more roundabout, the actual facts of the clearing process are enormously more widely operative in dealings between members of different nations than in dealings between members of the same nation. Within the national boundaries, there is, at any rate, a large volume of retail buying and selling for cash. Apart from the gold in the banks, there is in this country in the tradesmen's tills and in the possession of the people generally a quantity of coin of which it is difficult to form an approximate estimate—anywhere, perhaps, between one hundred and one hundred

and fifty millions—which is constantly circulating to and fro between consumers and retail traders. But the trading between nations is practically wholly of a wholesale character, and of articles of large values, as machinery, and so on. The quantity of gold occasionally changing hands between industrial nations strictly in settlement of trading accounts (apart from actual dealings in gold) is, relatively to the magnitude of the dealings, quite a negligible quantity—some half-dozen millions or so at the outside. The exchanges are effected by the medium of paper documents, analogous to the bank cheques so freely circulating at home.

Long before the banking system had developed to the extent that it has to-day, when every bank of any consequence has an agent in every important city all over the world, and can circulate "Drafts"—the equivalent of cheques—between the various places, there had grown up a vast system of dealing by means of Bills of Exchange—in effect, Promissory Notes. This system has grown up, not alone to enable dealings on credit, but so that the credit instrument—the Bill of Exchange—may operate as currency pending its period of maturing for payment in cash—a payment which, so far as being realised in actual practice, is a pure fiction. Thus, Carl Müller, in Berlin, sells goods to John Smith, in London, to the value of £100. He sells it on credit, but receives a Bill, promising to pay the amount in thirty or sixty days, as the case may be. In the meantime, he goes to his banker's in Berlin, and, at a charge of a small discount, can get that sum placed to his credit at the bank, on which he can draw by cheque in the usual way. Or the Bill can be passed from hand to hand, the claim for payment being transferred by endorsement—the essential quality of a Bill of Exchange. Müller is thus enabled to use the Bill before it matures for payment, for the purposes of his trade.

But, you may think, at any rate when the Bill matures it must be paid in cash. Nominally, yes; but practically, that very rarely happens. Thus, Carl Müller holds a Bill for £100 on John Smith, in London; while James Brown, in London, holds a Bill for £100 on Otto Heintz, in Berlin. The transmission of gold from one country to another involves cost of freight and insurance. But there is a less expensive way of settling the account than by sending gold. John Smith, who has to pay Müller, buys, at a small charge for commission, the Bill which James Brown holds on Heintz in Berlin, paying for it by cheque. He sends Brown's Bill to Berlin, when the account against him by Müller is cleared against the Bill for the same amount on Heintz, in the same city; while Heintz, who has to pay Brown in London, similarly buys the Bill which Müller holds on Smith, when his debt to Brown is cleared against the Bill drawn on Smith. Perhaps this will be made clearer by the following diagram:



The debts are simply transferred. Smith, who owes £100, instead of paying it to Müller, is authorised by him to pay it to Brown, in his own country; while Heintz, who is owing to Brown, pays it instead to his own countryman, Müller. The respective banks in each city, who are

instructed to collect the amounts represented on the Bills, now clear it against other paper documents in the usual course, and the debts are settled by entries in books. In effect, they are settled by "contra accounts," behind which are exchanges of goods for goods. The amounts of our trading with foreign nations go, in fact, to swell the total of clearings so astounding in their magnitude. In every important city there are a number of what are known as Bill Brokers, who make it their business to deal in Bills for settlement of accounts abroad, and sometimes issue Bills of their own with that object. They are, in effect, a species of Bankers; and it is they who are the principal borrowers from the banks on what is given as "At Call and Short Notice." Of recent years, the settlements in foreign trading are increasingly effected direct through the Bankers, who, in absence of the necessary Bills, can do so by means of Drafts on their Agents abroad. Thus, between people of different nations, as between those of the same nation—more so, in fact, between the former than the latter—exchanges of goods and services are effected without the use of a single penny piece.

Let us now revert for a moment to our tailor and grocer, whom we have supposed to be doing business with each other, and settling accounts *per contra*. The essence of such dealings consists in the fact that, at any rate, one of the two is willing to give the other credit—it can be assumed, e.g., that the tailor does not allow the grocer's accounts to exceed at any time the amount already standing to his credit for groceries supplied—or that they are both willing to give credit to each other. We may recall once more our supposed self-contained village community, constituting between them a complete circle of producer-consumers. If they all had perfect confidence in each

other's integrity, and provided that the demands for the products of each was somewhere about equal in value, they could be doing their buying and selling by means of contra accounts ; or if it were thought desirable to have some evidential records of obligations, it could be done by means of personal I.O.U.'s. Unfortunately, such universal integrity is as yet only a dream of the future, and with that there is lacking the confidence based on the belief of integrity. Nor would mere honesty of intention, and the belief in such honesty, quite meet the case. If Smith is to supply Brown with goods on credit, he not only wants to be satisfied that Brown intends to pay—in effect, that he will produce and give up for others to consume an equivalent of that which he consumed of the products of others—but that he will be in a position to pay when the account falls due. If Brown, with the best intentions in the world, should happen to be consuming (on credit) more than he is producing, or if the demand for his products or services should fall off for some unexpected reason, his honesty would be of little avail to Smith.

Suppose, then, that amongst our self-contained community—which for the purpose of our argument we may now conceive to be of much wider dimensions—there is one rich person whose ability to pay is unquestioned, in whom everybody has the most perfect confidence. We will suppose that he is a goldsmith by trade, who has for some time been engaged in lending cash at interest. Let us say that, apart from his stock in trade and other ample possessions, he has £10,000 which he employs in lending out, which, at an interest of 5 per cent. per annum, brings him a gross yearly income of £500. Presently the demand for loans begins to exceed the amount at his disposal for that purpose. Some pressing would-be borrower then urges the goldsmith to lend him his personal I.O.U., or

some other legally constituted document recording his obligation to pay on demand or on some stated date, knowing that such a document would be readily accepted in payment of goods. Having consented to such a course, the goldsmith finds that the document runs current—*i.e.*, is passed from hand to hand in payment of goods—for some considerable time before it is returned for payment ; and that long before it is so returned he was able to issue similar documents, which again run current for a considerable time. He thus finds that, in addition to lending his actual cash, he can also lend his "promises to pay," and so draw an income in interest on these as well as on the actual cash on loan. As a prudent business man, he would take care not to issue more of these "promises"—let us call them "notes"—than he can meet without undue strain on his general resources. Experience teaches him where to draw the line of safety against occasional exceptional demands for payment. The difference between the highest and lowest weekly average of the Bank of England note circulation in 1906 was slightly over 9 per cent. This is, however, a higher percentage than would be the case if the notes were of lower denominations—say £1 notes—which would remain in circulation for longer periods, with a smaller fluctuation. On our assumption that the confidence in the goldsmith's integrity and ability to pay is as complete as the confidence at present reposed in the Bank of England note, it would follow that on a reserve of gold of £1,000 (apart from the £10,000 in loans), he would be able to issue £11,000 in notes, thus drawing interest on a total sum of £21,000, instead of on £11,000, as would be the case if he only loaned his actual cash. Whether such a reserve trenches too near on the margin of safety is a question for bankers, on which something

further will be said presently. In this, then, we have two most important results: the quantity of currency in circulation so far as this particular issue is concerned is just on doubled; and the goldsmith is able to draw an income for providing a medium of exchange which does not consist of coin at all, but of mere pieces of paper recording promises to pay, which in fact never are paid in cash, since the quantity of notes presented for payment are, to within a fluctuating margin of 9 per cent, always covered by new issues to the same amount, so that it is merely a matter of paying to one while receiving from another, like the gold circulating in and out at the banks' desks.

Our goldsmith is no mere figure drawn for the purpose of illustration. He was in reality the actual originator of banking during the Middle Ages. From being only a money-changer, dealer, and then lender, he presently became a borrower as well as a lender; while many were glad to deposit their cash and valuables with him for safety. The receipts held for such deposits were probably the earliest form of paper currency. Borrowing at a smaller interest than he was lending, just as our bankers do to-day with what is called the "deposit" accounts, the goldsmith was able to make a handsome income out of money borrowed and that entrusted to his keeping. In course of time a system of banking was gradually developed, out of which our present exceedingly elaborated system of banking has slowly evolved to its present gigantic dimensions. The striking developments date, however, from the legal institution of banking by joint stock companies.

We are now in a position to understand—as yet, perhaps, but imperfectly—what it is that the bankers are lending. The man in the street has some hazy sort of

notion that, when one borrows £1,000 from his bankers, he brings some canvas bags and carries off the amount in gold, or at the very least in bank-notes. But, except only in cases so very rare as to be quite negligible, nothing of the kind happens. I am not at all sure that anyone could borrow such a sum in gold without notice; and I am confident that the kind of borrower who would want to do this is rarely one with whom banks would have dealings. All that takes place is that £1,000 is placed to his credit on the bank's ledger, and he is then in a position to draw on the bank for that amount by cheque, as required. Let us suppose that he wants the whole sum in a lump to pay off a mortgage, or a bill which falls due. He draws a cheque which says: "Pay John Smith the sum of £1,000." But John Smith does not take the cheque to the bank, demanding the amount in gold or notes. He pays it in to his bankers, authorising them to collect the amount for him. John Smith, particularly if he is engaged in trade or business—and it is people so engaged who are the principal borrowers from banks—has also various sums to pay out, which aggregate somewhere to about an equal amount. His bankers clear the cheque paid in by him, not necessarily against the very cheques paid out by Smith to sundry creditors of his, but against any other cheques, drafts, or bills, held on them by the bankers on whom the cheque payable to Smith happens to be drawn. It requires, however, but little imagination to realise that, in the course of clearings of the various banks one against the other, the cheque in favour of John Smith does, in a more or less roundabout way, get cleared against cheques or bills paid out by Smith in the course of his business or private debts. But, the critical reader will say, while that sum of £1,000 remains on loan, though consisting in the first instance of no more than a mere credit entry in a ledger, if that credit

is drawn upon, there would be that much of adverse balance against the lending bankers in their clearings against other banks. Well, there would be if the other banks did not lend also ; but when they all lend, there is no adverse balance other than the usual fluctuations this way and that. Thus, *e.g.*, Lloyds lend to Smith, and Parr's lend to Brown. Now, if we suppose that Smith borrowed to pay off an account due to Brown, while Brown borrowed to pay off an account due to Smith, there would obviously be no adverse balance between Lloyds and Parr's. But though Smith actually pays Jones, while Brown pays Robinson, the cheques will nevertheless get cleared against each other, and there will be no adverse balance between the banks, except only to whatever extent one bank may be contracting an altogether unusual amount of loans—a course which sound banks in this country are not in the habit of doing.

Against the credit side granting the loan at each bank, there is a debit entry on the opposite side, recording the loan. When this is paid off, also by cheque, draft, or bill, which the borrower has been enabled to obtain in the course of his trade by means of this very loan—the credit currency which enabled him to keep his factory or business in going order, or which, by enabling him to meet some pressing obligation, prevented a collapse—the account is balanced, and there is an end of this transaction. No, not quite an end. Production has been kept going by means of a credit currency ; there has been an increase of utilities for human consumption ; goods and services have changed hands without the medium of coin. But the providers of the credit currency—the tool by means of which the exchanges were effected and production kept going—claim a share of the utilities created in return for having provided the factor without which, in

the conditions prevailing, the production could not have taken place. You may call it interest, if you like ; but so may the miners' wages who dig the gold used for currency be called interest. Both are the producers of tools necessary under given conditions. Whether the plane used by the carpenter has a wooden block or a platinum block may make no difference to its efficiency as a cutting instrument ; and the provider of the plane is not the less entitled to a share of the product in part created by the tool which he has provided because the block is made of wood instead of platinum. Indeed, the organisation of banking which provides in effect a safe paper currency, to take the place of a metal currency to the extent, probably, of no less than 200 to 1, provides an instrument without which production could not have arrived at its present state by many thousands of miles. As has already been elaborated in considerable detail, division and specialisation, which are the very life of production, could never have taken place without the invention of a currency of some sort. But the measure and efficiency of that division and specialisation must obviously depend upon the sufficiency and efficiency of the tool employed. Just try to imagine what would happen if the exchanges represented by the fifteen to twenty thousand millions of clearings in this country alone had to be effected by the medium of gold ! There is probably not half that quantity of gold in the whole world, even if we allow for secret hoardings. Of course, such a contingency is simply unthinkable—impossible. Had man failed to invent a credit currency —were men dependent upon gold and silver alone as their medium of exchange—production could simply not have arrived at its present stage. It must have remained, at least, in the elementary conditions of medievalism, or even something much more primitive, since even medievalism

was not entirely without its banking facilities and the means of trading on credit.

All this is not meant to convey that banking is entitled to be a privileged monopoly. Whether quite as efficient and effective an organisation could be instituted in such a way as to reduce the scarcity conditions, and consequent rent of monopoly and special ability accruing to the providers of the currency of commerce; whether even a better organisation for the provision of a currency could be arranged on wholly different lines: these are pertinent questions which will demand our serious consideration at a later stage, when we are further advanced in our investigation. For the present what is essential for us to realise is, that the notion that bankers are money-lenders in the ordinary acceptation of the term is quite a wrong conception of the bankers' functions. Bankers are the actual creators of a currency system which takes the place of a purely gold or silver currency—a system which, as compared with the latter alternative, is so much the very life-blood of modern methods of production that a reversion to a metal currency alone is simply unthinkable to those who realise the nature of modern production and exchange. As such, they are not merely the providers of a tool which could be equally provided by any Tom, Jack, or Harry—the gold-mine owners, for example—but are the real owners of a monopoly in organising ability which is both unique and quite indispensable. Whether that unique organisation could be taken out of their hands and placed under collective national control—Government department of credit and banking—without disaster to the elaborate and delicate mechanism, whether certain legal modifications would improve the mechanism left in the present hands, are different questions which do not affect the true conception of the function of banking.

I fear, however, that I have allowed myself to anticipate considerably beyond the stage reached in our investigation of the currency problem. Whatever appears to the reader still obscure and unconvincing will, I trust, be gradually made clear and convincing as we proceed to unfold the various aspects in succeeding chapters. An adequate treatment of this great problem in all its bearings is, of course, out of the question in a general outline of the economic framework of such limited scope as this treatise. Nevertheless, I am fain to hope that the essential features necessary, not to a knowledge of the art of banking and financing, but to a general understanding of the main economic issues involved, will stand out sufficiently bold and distinct to give the reader a firm grasp of the problem as a whole, and to whet his appetite for further study.

CHAPTER XI

SOLVENCY OF BANKS—PSYCHOLOGICAL BASIS OF CURRENCY—NATURE OF SECURITIES—FINANCE INSTRUMENTS TRAVELLING UP TRIBUTARIES—PRODUCER-CONSUMERS—WAGES FUND—THE ECONOMIC ILLUSION OF AN INVERTED IMAGE

We have seen that, except for a sum so small relatively to the amount out on loan as to be negligible, the bankers lend nothing but their credit, or promises to pay, which in fact they are never called upon to pay in cash. The reader will also have been struck by the fact that against a liability of one thousand millions they have no more than somewhere about one hundred millions available; and of this the bulk remains practically constant in the banks. I know that this is one of the things difficult of assimilation by one to whom the fact comes as a surprise. "Nonsense!" I heard one such exclaiming; "do you mean to tell me that if I had a cheque on one of the reputable banks, no matter for what amount, I could not get cash for it?"

Well, now, let us follow up the matter a little farther. Against the thousand millions of liabilities, there are seven hundred and thirty-five millions ($\text{£}735,000,000$) owing to the banks for loans; and as the people who hold the credits on the banks are also the very same people who hold the loans (it must be remembered that we are dealing

with the bulk of the leading banks collectively), the actual liabilities are reduced to two hundred and sixty-five millions ($\text{£}265,000,000$). This, however, does not quite clearly convey the actual possibilities of the case. Of the $\text{£}735,000,000$ on loan, $\text{£}110,000,000$ are at call and short notice. To the extent of the latter sum, therefore, there can be no sudden call for gold. But as to the other $\text{£}625,000,000$, theoretically, people may, under the emotion of panic, demand gold for whatever stands to their credit on the books of the banks, spite of being themselves indebted to the banks for loans, the repayments of which are not due for days, weeks, or months, as the case may be. Practically, however, in the supposed case of panic, a borrower would be only too glad if the account standing against him were cancelled against the credit in his favour. For practical purposes, then, we may take it that the theoretically possible danger of a rush for gold on all the banks at the same time applies only to the $\text{£}265,000,000$ not balanced by credits on loans, thus leaving a possible demand for gold to the extent of $\text{£}165,000,000$ for which there is no coin or bullion whatever in hand. This is modified to an extent by the fact that most "deposit" accounts are not payable on demand, but are subject to seven or fourteen days' notice, as the case may be, so that during that time assistance may be rendered by bankers abroad. On the other hand, there are the seventy or so other British banks, as also some eighty foreign and colonial banks who have business premises in London, of whose cash and liabilities no figures are available. We may put it down, then, that the possible call for coin in case of general panic exceeds all the available coin and bullion in the hands of the banks in this country by something like $\text{£}200,000,000$. This takes no account of the Government Savings Bank deposits. Such a sum is easily enough

spoken or written, but is one of great magnitude in such a case as we are supposing.

If the reader will turn back to the banking figures, he will see that the commercial solvency of the banks is not in question. Against the net balance of callable liabilities for which no cash is available, there is £255,000,000 invested in public securities held by the banks under review, and sundry other assets ; in addition to which there is the considerable liability of the shareholders on uncalled capital. But all these do not alter the proportion of coin and bullion to liabilities, and are of no avail whatever in the supposed case of a sudden rush for payment on all the banks at once.

Now, modern banking is, as we have seen, mainly a system for the provision of a paper currency, and, like the problem of currency as a whole, it is almost entirely a problem in human psychology. The actuary works out his life insurance premiums on statistical records of the average duration of life. In the case of any one individual life, such a calculation would be a sheer gamble, but when a large number of lives are taken together the averages are reliable almost to a day. Nevertheless, a sudden epidemic may ruin the insurance companies, and yet not in the least invalidate the actuarial figures based on normal conditions. Now, just as the insurance company bases its expectation of life on a known average under given conditions, so the banker bases his expectation of human conduct on the known average of conduct under given conditions. The banker is not the only one who does that ; each one of us goes about his daily life and avocation in the full and confident expectation that his fellow-men will act as he knows them to be in the habit of doing ; that conduct is the outcome and expression of motive ; and that in all normal and more or less ordinary conditions and

affairs of life the motives and desires which are the main springs of his own conduct are equally the controlling force of the conduct of others. One goes to his barber to get shaved without fear of having his throat cut. One walks out in the street without the expectation that his fellows will run amuck. One sells on credit in the firm conviction that his debtors will not all go bankrupt at the same time. And yet now and then someone does run amuck ; some barber may go mad and cut a customer's throat ; some unforeseen commercial or monetary crisis may cause an abnormal number of bankruptcies. As far as conditions are known, the exceptions are fairly well marked. Policemen are said to perambulate in couples in certain streets inhabited by a dangerous class of criminals. The man who walks without qualms in Oxford Street may not feel quite so confident in some back street in Limehouse. But these exceptions do not affect the average of conduct, any more than the sudden death of an apparently robust young man affects the average duration of life.

The banker knows that the desire to hoard gold has almost completely died out amongst the well-informed and well-to-do classes in all civilised countries ; that, on the contrary, men are anxious to deposit with bankers whatever cash they have beyond immediate requirements. In proportion as a nation is in a stable condition, and is at peace with its neighbours ; in proportion as production is proceeding uninterruptedly, and obligations are enforceable by law without fear of bribery ; in proportion as there is confidence in the honesty and solvency of bankers, and the financial mechanism runs smoothly, the desire to materialise one's credits into hard coin does not arise. It is only when confidence is shaken that men rush to what they conceive to be the irreducible minimum of security. With the exception of the comparatively few millions

circulating to and fro, mostly in a weekly cycle, between banks and their clients, for the purpose of paying wages and for retail purchases, men neither pay gold into the banks nor draw gold from the banks. They pay in transfers of credits to their own accounts on the bank's books from the credits of the accounts of others on the books of the same or other banks, and they pay out by reducing their own credit, which is transferred to the account of others. But, as the result of this juggling with numerals, products and services are created and change hands. I can fancy many a simpleton—as I indeed know to be the case—imagining that the cheques, bills, notes, postal orders, and other paper documents paid into banks, get converted by some esoteric process into golden sovereigns, which are kept in the banks' vaults pending the depositors' orders, and that, when a cheque is paid out, so much gold is taken from the hoarded pile and given to the holder of each cheque. But nothing of the kind happens. There is sufficient gold in the banks to meet what experience has proved to be the average demand, and something over for ordinary fluctuations or trade emergencies. There is gold for all who want it, provided all don't want it. A run on any one bank, granted that the position of the bank is perfectly sound, would be only a temporary inconvenience, as all the other banks would come to its assistance. But a run for gold on all the banks at the same time would soon run the fountain dry to aridity. The misfortune of such a case would be, not that anyone with a legitimate claim need necessarily be denied real satisfaction of his claim—real, that is, in actual wealth for consumption—but that, in the temporary breakdown of the machinery which keeps production in motion, production itself is arrested, and so much wealth which might have been created is lost to the nation and to the world. The currency

machinery is, in effect, a "confidence contrivance." The actual leverage which manipulates the mechanism is really the transference of claims on production from one to another, by means of legal instruments of indebtedness, recorded in various ways; but screening the actual process is the convenient fiction that each claimant has so much gold awaiting his disposal, and that it is by means of this gold that he accomplishes his buying and selling, and his investing in all sorts of securities, shares, and companies. All this is a sheer delusion, which we shall realise more clearly as we proceed.

The complete solvency and standing of the banks is secured, as we have seen, by their investments in certain public securities, of what is known as the "gilt-edged" type. But their own investments, amounting to £255,000,000, is in reality a mere fraction of the securities guaranteeing their solvency. The £750,000,000 which the banks under review have out on loan are advanced on more or less similar securities owned by their borrowers, which are pledged by contract to the banks, entitling them to realise the securities at the market price of the day in the event of their clients not meeting their obligations as due. A bank which launched out in lending largely on mere personal promises to pay, or even on ample security of property not readily realisable in open market, would, were the fact to become known, incur a serious danger of a run on it for gold. Hence, practically nine-tenths of the bankers' assets may be said to consist of securities.

Now let us see what are the nature of securities. Certain municipal securities provide for the repayment of capital, but this is spread out over a long period—generally sixty years. National securities, such as Consols, for example, contain no undertaking for the redemption of the capital. At any rate, neither of these are promises to

pay any sum whatever on demand, beyond the stipulated annual interest. In the case of such securities as railway, electric, gas, water, and other stock of a similar nature, and of shares in companies of all kinds and conditions—industrial, gold, silver, steel, copper, rubber, oil, and what not—they constitute part proprietorships in the undertakings, entitling the holders to share in the profits, if any. They are all simply liens on future production. None of them are convertible into cash as a matter of right, but, when the concerns are sound, they are said to be saleable on the market—*i.e.*, the Stock Exchange. Here we get the same confusion of thought with which we are already familiar in the case of banking—only much more so. When it is remembered that the quantity of supposed saleable securities amount to such a phenomenally incomprehensible sum that even the staggering sum of bank clearings are the merest bagatelle by comparison, the notion of their convertibility into gold stands out as the grotesque fatuity of a demented golliwog. You can find buyers—at a progressively descending scale of prices—so long as there are relatively few sellers. And the cheques which you receive in payments for the stock you may, if you like, convert into gold, so long as there are not many sellers wanting to do the same. Long before the time that the sellers became so numerous as to cause a drain on the available gold, the stock will have become unsaleable at, practically, any price. Like all the rest of the currency and financial problem, it depends upon a mental balance being maintained, as a result of conditions governing the mind operations. Not that any one has worked out in theoretical detail the psychology of the matter. It is arrived at empirically, but none the less surely for that. It is the "psychology of the crowd" that is the most baffling, mysterious, and impossible of prevision; and the

only effective remedy is to keep the causes of contagion—mainly arising from too speculative dealings—as far off as possible.

Securities, then, are legal documents pledging the future production of the people of a country. In the case of public securities, the State enters into contracts to tax the future earnings of the citizens, to a stipulated annual sum for the benefit of the security-holders—in effect, that, out of what is being produced from year to year, a certain share will be taken from the producers and given to be consumed by the holders of the securities. In the case of shares in joint stock companies, the contracts are to share "profits" among the shareholders—in other words, that, out of the utilities created by the workers in the respective industries, whatever remains after the workers have received their stipulated share shall then be shared out amongst the holders of the share certificates. Within narrow limits, securities will command buyers in proportion to the confidence reposed in the honesty and ability of the contracting parties to carry out their obligations, and (in the case of profit-sharing) in the capacity of the industry to leave a balance for the shareholders. But, in the very nature of the terms employed, finding a buyer means that, in place of A holding the lien on future production, it is now transferred to B, while A gets from him either cash for conversion into consumable things, or—which is mostly the case—some form of credit that gets converted into utilities in the course of the bankers' manipulation of the credit currency. Whether held by A, B, or C, the securities remain always liens on the future industry of mankind—claims to share in the products created from day to day by the hive of human producers. The securities will "secure" nothing except what human effort creates out of the materials supplied by Nature.

The bankers' currency is, therefore, based primarily on their holdings of contracts constituting liens on the future production of wealth. Some nine-tenths of their assets consist of such contracts, and thus form the foundation of the trust reposed in them. It is as a consequence of holding these legal pledges on the production of futurity that they are able to float a vast system of bank credits, which perform the function of a currency for the interchange of products and services all the world over. Behind that is a comparatively small fraction of a metal currency, which, besides its necessary use in cases where a credit currency is found impracticable under prevailing conditions, serves also as a "confidence contrivance"—a convenient fiction. The quantity of metal currency in use in proportion to credit currency, relatively to the total of exchanges, varies in different parts of the world, depending upon the degree to which the people of the district have acquired confidence in banking credits, and to the extent that they have learnt to avail themselves of banking facilities. Thus, good harvests in India, Egypt, Argentina, Brazil, and so on, will make very considerable calls on gold and silver money for settling accounts; while a prosperous year of industrial production, *e.g.*, in England will, in proportion to the increase in the total of transactions, make but an insignificant additional call on gold. But the increase will be strikingly noticeable in the clearing houses. Some nations have not grown out of the desire to hoard gold; and the more prosperous they are becoming, the more of the precious metals they are absorbing for the purpose of hoarding. Thus a considerable quantity of gold gets extracted from the bowels of the earth in one part of the world, only to get buried again beneath the earth in another part of the world. The question of money is purely a question of "confidence." Anything is good money provided the

confidence in its functioning as money is complete, and it is the problem of maintaining that confidence intact which constitutes the most difficult problem in the whole range of modern economics. We shall see this more clearly when we get to our final analysis of the nature of money and the problem of modern currency.

We can now follow in more detail our diagram of products travelling down the stream from a great number of tributaries, and of instruments of currency travelling in the contrary direction towards the sources of the tributaries. The reader of course understands that the trades are just roughly divided up for the purpose of illustration, without any pretence to accurate classification. Consumers at the mouth of the stream draw from it, say, a number of pairs of boots, for which some pay in cash and others by cheque. The boot-dealer pays both in to his banker's, and gets credit on the bank's books. Now, every reader is well aware that in practically all but strictly retail trading, and to a very large extent in that also, it is the universal custom to give credit, generally on monthly accounts, but often for longer periods. In some cases they are ordinary book credits, but in others the debtors "accept" bills, payable in thirty, sixty, or ninety days, as the case may be. We already know the nature of bills, and that they are frequently used for procuring "advances" from banks—that is, the limited credit of the individual or firm is converted into the current credit of the bank. In such cases the sellers obtain immediately on the sale of their goods credits upon their bankers, on which they can draw for meeting any demands upon them.

What takes place, therefore, is this: As the goods in the various stages on their way to becoming commodities travel down the tributary from breeder to tanner, from tanner to currier, from currier to bootmaker, and from

bootmaker to consumer, cash and credit documents pass from one to the other in the opposite direction. The consumer, whether he pays in cash or by cheque, has to pay the whole of the labour value embodied in each pair of boots, from the breeder down to the porter who delivers them at his door—including the claims of land, of capital, and of organising ability. The bootmaker, converting the payments of his retail customers into bank credits, first of all draws sufficient in cash to pay his wages bill, and his personal requirements. On the credits still remaining to his balance he draws the monthly cheque, or cheques, as accounts become due; or if he has "accepted" a bill, the credit is there to redeem it as it matures. The bill, when "accepted," or the cheque, when drawn, travels to the currier, and is paid to his bankers, thus creating a bank credit in his favour. The currier, in his turn, draws on that credit for paying his wages bill and personal expenses, and for forwarding a credit document to the tanner; and the tanner, in his turn, transfers a part of his bank credit on to the breeder. As these credit documents pass up from consumer to breeder, the amounts become smaller at each transfer of credit, relatively to the retail sales which they represent, the bank credits created by the payments of the consumers becoming lessened at each stage on the way up by the shares due to the factors co-operating at that stage; and, conversely, the value of the goods is increased at each stage on the way down, by added claims of the factors contributing in the gradual conversion of the raw material into the finished product available for consumption.

But now we must realise that the producers are also the consumers—that they are not two different sets of persons, but one and the same set. (Such of them as do not produce any useful service whatever, being what are

called "necessary factors of production," as legal owners of land and capital, must, for the purpose in hand, be classed as producers.) If, then, we were to draw sweeping curves from each of the trades in the course of the various tributaries, all converging to the mouth of the stream, we should get a mental picture of what is taking place. Wherever we begin, it will be a "beginning from the middle," as it were; so the reader must make allowance for some little redundancy or strain in expression. Let us, then, begin from a point when each one of the many co-operators in the production throughout all the processes in all the industries—landowners, capitalists, employers, manual workers, managers, and organisers—is in possession of claims on production, as a result of having contributed something to the stream in the past, which had been consumed by another; in return for which the latter gave up an equivalent in claims on production—money or credit—which went to the provider of the utility which he consumed. All go to the mouth of the stream, drawing from it such utilities as are there available, to such value as they need at the time, or to the full extent represented by the total of claims in their possession, giving up in return an equivalent of the claims, which are sent off on their journey up the tributaries. While these claims are in course of transit, production continues, and at each stage in the various processes, at certain customary intervals, part of the claims making their way up is abstracted and redistributed amongst the people who have but just before parted with these very claims, in the act of becoming consumers, but who have since become entitled to them once more for having already made further contributions of what will later again emerge as finished products at the mouth of the stream. And so the claims become once more available for drawing

utilities for consumption from the stream ; but no sooner do they perform that service than they once again start on their upward journey, to be once more redistributed in various proportions amongst the many contributors to the stream of production. We say that "money circulates." It does indeed perform a complete circle, playing the part of a "medium," instrument, or contrivance, by means of which the utilities being created are apportioned amongst the various contributing factors in such shares as the economic conditions enable them to command.

We are now in a position to resume our consideration of "capital" from the point where we left it at the conclusion of Chapter IX. Hitherto we have purposely limited our conception of capital to the tools and implements of production, with but just the barest reference to yet another form of capital requisite to production. We were not in a position to follow the latter clearly, and without the risk of an entirely false conception, until we had made ourselves familiar with the financial process employed.

Apart, then, from the buildings, tools, machinery, and other implements, and also the requisite stock of raw materials for conversion into goods—e.g., the ore for smelting into iron, the iron for hardening into steel, the steel for making up into cutlery—the employer in each trading unit must have a fund of money or bank credits for wages or other immediate outgoings, sufficient to last until the first consignment of completed goods has been delivered to the employer in the next succeeding process, or until the account for payment falls due ; when, either by bill or by cheque, his credit at his banker's, depleted by the outgoings, will be restored to not less than it stood at the start. To get this clearly, let us illustrate it by some concrete figures. Suppose that monthly accounts

are the custom in that trade, and that the weekly wages bill and other outgoings is £100 per week. Assuming that the process is not a protracted one, as in building, elaborate machinery, and so on (where, however, periodic payments on account is the invariable rule), and that the accounts are paid regularly somewhere about the 10th of each month, the employer must start with a credit at his banker's, roughly, of about £600, to last him until the batch of cheques in settlement of accounts is paid in. If the custom is to take bills, which are discounted at the bank, and the process of manufacture is a short one, then anywhere from £100 to £300 would probably somewhere about meet the requirements of the case. Once the industry is in full swing, batches of goods keep on going out daily as they become finished ; and so each daily bill or monthly settlement supplements the credit depleted in payment of wages and other outgoings. But the credit at his banker's need be no more than borrowed credit, raised on quoted securities, or even on the security of his business premises, machinery, and plant, at an interest of from 4 to 5 per cent. per annum ; thus, at a cost of from £5 to £30 per annum the banker will provide him with a credit currency necessary to carry on his business. If he is a merchant doing business in the City on a large and fluctuating scale, it may be that he is invariably dependent on his bankers for the credit requisite to business. The wages and outgoings fund is then reduced practically to nil.

We should now be in a position to take a full and comprehensive grasp of the economic reality of the forces governing the productions of utilities, without being so egregiously and constantly deluded by the currency mechanism into seeing a completely inverted image of

the real process. But, much as I should like to flatter myself into the belief that my capacity for convincing exposition, and the avoidance of such terminology as tends to foster the illusion, has by now quite dissipated that danger, I am nevertheless conscious that a conviction so deeply rooted and so widely prevalent is not likely to be shaken off without considerable mental discipline. Long as I have been aware of this all but universal illusion, and much as I have noted its intensity and persistence, I am even now taken sometimes by surprise at the crass stupidity and utter lack of receptivity on this subject even amongst well-educated men. Go where one will, in the city or suburb, the train or the tram, the hotel, restaurant, or public-house, from platform, pulpit, and press, the illusion is persistently and glaringly in evidence. Some men are said to need an operation to make them see a joke. It would need an entirely new brain to make most men give up this much-cherished illusion. Some illustrations of this have already been given; but partly in order to help the reader to a more complete emancipation, and mainly by way of preparation for what will follow presently when we come to discuss the faults of the present system and to consider possible remedies, it will be necessary for us to do our best to choke the monster completely out of existence, without risk of resuscitation.

Only a few days ago I happened to be listening to a friendly chat amongst a number of prosperous City men over a cup of tea. When I became conscious of their conversation, one man was saying: "Oh yes, I have heard these sort of arguments before. One coal-merchant, they say"—I did not catch who the "they" were, but took it to be the Socialists—"sends a load of coals from Willesden to Brixton, while another coal-merchant sends a load of the same kind of coals from Brixton to Willesden. The

men and horses pass each other on the road, trudging, perhaps, a whole day, wearing out horses, carts and harness, clothes and boot leather" (human lives cost nothing, so they don't count); "though the work could have been done in an hour or so by each merchant serving in his own district. How absurd! Are not these men earning their living? Aren't they getting wages?" "Oh yes," said another, "I've heard this argument applied to milkmen. There are, perhaps, a dozen of them dodging in and out of gates in the same road, skipping some and crossing from this side to that and back again, some with horses and carts, some with hand-barrows, some merely carrying cans in their hands; when, if only properly organised, two or four men with the aid of well-equipped vehicles could do the whole work with no greater expenditure of time and effort than they are giving now. This is all very well; but they are overlooking the important fact that these men are all earning a living." There was apparently complete agreement amongst them on the point.

It is quite a common thing to hear in the City a fall in the value of public securities spoken of as a loss of so many millions—not to the holders of the securities, which is true enough if they should want to sell them—but as a loss to the nation. But the nation pays the same interest on the nominal £100, whatever its quotation on the Exchange; and in the event of reduction of the debt by purchase in the market, the fall in price is a distinct gain to the nation as a whole. Consols cannot be lost, as their ownership is merely inscribed on books at the Bank of England; but if national bonds to bearer were entirely destroyed, while the owners would, of course, be losers, the nation would be the gainer, by not having to pay the interest. (There are, of course, indirect consequences of

such individual losses, which may interfere with production, but this is another matter.)

There is a well-known story, which has done endless service, of a Socialist who went to Rothschild's demanding a share of his wealth, on the ground that wealth should be equally divided. Rothschild is said to have taken a pencil, and, dividing the sum of his wealth by the number of inhabitants in the world, found that the share of each would come out at a half-crown. "Here, my friend," said Rothschild, "is your share, and good-luck go with you." The laugh comes in here, on account of the share being so small. Had it been half a million instead of a half-crown, then the laugh would have been the other way about. This reminds one of the story of the kind-hearted old gentleman who had a scheme for entirely abolishing poverty in the course of one hundred years. All the Governments of the world were to impose a special tax during one year, which was to be known as "The Fund of Futurity." This was to be invested at compound interest for one hundred years, his estimate being that at the end of that time the simple interest on the accumulated sum would be so immense that it would provide a sufficient income for every man, woman, and child, in the world, when the need to labour will have entirely disappeared! Put in this way, even a child can see how grotesque is the notion of "living" on a money income—how the fact that one consumes without producing must mean that someone else is producing it for him. Yet the Rothschild story, which has provided many an honest laugh at the expense of the ridiculous Socialist, is exactly of the same calibre. Provided the share of everyone had proved to be half a million, yielding an income at 5 per cent. of £12,500 per annum, then the Socialist would have been a very smart fellow, and everybody would have lived happy for ever

after. As we go along, we shall see it standing out clearly enough that it is only by some having much claims on production, and others less or none, that the claims—whether in cash or in any other form—are of any consequence. If all had an equal amount—whether the half-crown estimated by Rothschild or the straw-Socialist's dream of half a million—it would, apart from its convenience as counters for effecting exchanges, be utterly worthless and meaningless as an object of wealth (other than its use in the arts). If I can call upon you to do a day's work for me because I have so much money, and you can call upon me to do a day's work for you because you have as much money as I have, then the best thing we can both do is to throw the money into the sea, tuck up our sleeves, and just do for ourselves and for each other as much as is needed to get the best out of life.

But the widespread extent of this conception of income has been most strikingly illustrated during the last ten years, in the controversy over the present movement for a return to Protection. Whatever economic arguments of any degree of validity there may be in favour of Protection (we have nothing to say to that at the moment), in its appeal to the working man, the salaried clerk or assistant, the small tradesman, and the man in the street generally, there is one, and only one, argument that stands out clear and unmistakable—without which, indeed, the proposal would be quite meaningless. "There are a great variety of things," says the Protectionist, "coming here from abroad, in large quantities, which could very well be made at home. The people who make them receive wages and salaries; the manufacturers and dealers make profits. Why, then, not make them here, and so put the wages, salaries, and profits, into the pockets of our own people, instead of into the pockets of the foreigners? Put a tax

on imports, so as to stop them from coming in, and let the things be made here instead ; and so provide work and wages for those now unemployed." That the Protectionist expects both the revenue from the taxes on imports and the plethora of employment created by keeping the imports out does not concern us at present. (It should be noted that the revenue from taxing imports is generally estimated by the Protectionist on the present figures.)

Now, what is the Free Trader's reply to this contention ? He says that for the things we get from abroad we give in exchange, not money, but other things which are made at home ; that, if you cease taking the things which now come here from abroad, the foreigners will then be compelled to cease taking the things which we now give them in exchange for what they send to us ; and that there could be no increase in employment or wages, since whatever we should gain in the making of the things which we are now importing would involve a corresponding loss in ceasing to make an equivalent of those things which we now export in exchange for the things imported.

Now, I cannot recall to mind a single speech or argument from platform, hustings, or street corner, a single article, paragraph, or sentence, in the Free Trade press or pamphlets—and I have heard and read as much as most men on this subject—which pointed to the complete travesty underlying the Protectionist's contention as it stands. By common consent, it is apparently agreed that what men require is a money income, obtained no matter how—be it in the form of wages, salary, interest or profit, by needlessly duplicating labour, by doing each other's washing, by ploughing the sands on the seashore, by getting it out of the pocket of someone who happens to have it, by any device or inducement : anyhow, somehow, so long as you get it. If it were realised—I say "realised,"

not merely subscribed to as an economic formula—that men's incomes consist of utilities, of things to consume, then the Protectionist's argument would at once stand out as a glaring absurdity too puerile for serious reply. "Here," he says, "are things coming in. But I hold that they ought not to be allowed to come in, but that we should be employed in making them ourselves." All right. And when you have made them you will have—what ? The things. Very well, here are the things—you say they are coming in. What is the point in making them if, as you say, they are here already made, available for consumption ? I will not pursue the point farther ; for if the reader who has been interested enough to follow me so far cannot see it at a glance, I am afraid he is very nearly a hopeless case.

But, obvious as it may now be to the reader, it is no easy matter to make the average man see the point at all. The "Free Trade Union" is apparently quite unconscious that there is anything at all unreasonable in refusing to have a thing already made, so that by expending much labour one may earn wages for making it—and then expend the wages in buying the things back for consumption ! And so, starting by conceding this piece of egregious nonsense, they go on for ever spinning figures to prove—this, that, and the other. Those publicists who, *e.g.*, like Mr. Chiozza Money, are well aware of the economic truth, are probably of opinion that it is not an argument that would be understood by the crowd, or by even any appreciable section and in this they are undoubtedly right. The great bulk of people are still steeped to the lips in the mercantile theory of wealth ; or, rather, they have no theory beyond the inherited, instinctive conviction that money is wealth, and the only source of wealth.

Let us now take another striking example, which I am

giving with some reluctance. Owing to its connection with current politics, and the use of actual names, although it is a matter of public knowledge freely handled in the press, it is liable to arouse prejudice and suspicion of conscious bias. The lessons, however, which we can learn from these examples are too important to be missed; and I can only promise to do my best to deal with the matter in such a scientifically impartial spirit as I am capable of, having strictly in view the economic investigation we are engaged in.

During the great Budget agitation of 1909, the conception which sees an inverted image of the economic reality has had many notable exemplifications. On behalf of the Duke of Devonshire, it was publicly urged, in the Duke's presence, as a reason against Mr. Lloyd-George's Budget, that, being an extensive breeder and runner of race-horses, the oppressive taxation may result in the Duke reducing or giving up his stud altogether, which would throw a number of men out of employment. The Duke of Northumberland wrote to *The Times*, I doubt not in all sincerity, that the particular luxuries he indulges in are deer-parks and ornamental gardening; and that the additional taxation will compel him to give up some of these, thus throwing a number of men out of employment. Quite a number of other Dukes and Lords followed in the same strain.

Now, this is not the place to discuss the ethics of horse-racing. The point is, that there was obviously no attempt made or intended to defend the practice of horse-racing, with its attendant consequences; the proposition being simply that it provides employment at wages, and that that was the first and last word that need be said on the matter. In countries where they have gambling-places of other kinds—casinos, lotteries, and so on—exactly the same defence is made when their abolition is advocated. The

maintenance by these Dukes and Lords of a large number of flunkies, manifestly as traditional symbols of pomp and ostentation, who have practically no really useful service whatever to perform, is pointed to as a public benefaction, inasmuch as it provides a number of people with food, clothing, and good wages. Not for a moment does it seem to occur to them that others must be labouring to produce the things which the flunkies are consuming without giving any useful return, and that, were they also engaged in producing, there would be that much more of utilities to go round. It does not seem to have at all occurred to the Duke of Northumberland that it is quite possible that both his dismissed keepers and the nation at large might be largely the gainers if his deer-parks were converted into farms and small holdings. That under present conditions of ownership and industrial organisation it is distinctly true that it is often better that the noble lords and their imitators should keep an array of virtual idlers, rather than they should be thrown on the streets, while access to land, implements, and industry, is denied them, does not in the least alter the economic truth that money wages is not the income on which men subsist; and that subsistence without production, no matter who pays the wages or where it comes from, can only be accomplished by taking the products created by producers and giving them to be consumed by the non-producers.

One more example must serve as the apex of our present structure, not because the view expressed is so much more stupid than the rest, but because it comes from a source held in much esteem by all sections as a very ably and carefully-conducted journal. The paragraph stands quite alone, so that there is no question of "context":

"There are many complaints as to the increasing cost of living. An American writer in the *Atlantic*

Monthly suggests a cause which is devoid of reason. We are paying not only for the simple goods we require, but also for the shop-windows in which they are gorgeously displayed, just as we pay not only for the food and drink we require, but also for the elaborate and unnecessary appurtenances which surround and embellish them. In short, we cannot buy a cheap pair of socks without paying our share of the cost of the expensive emporium in which they are displayed. It is a sad and sorry fact of life that we cannot get anything at the bare cost of production. But if we could, we should neither want things nor have the wherewithal to get them. The temptation of the shop-window is at the basis of civilised life, which wants and supplies unnecessary things. Who would know a cutlet from a chop without its frills? We pay for the frills—and live on them."

This is almost—not quite—worthy to rank side by side with the silver-lined cloud of crime, which gives employment to policemen, prison-warders, and so forth. The crime and the useless frills both provide employment for money, which constitutes the "wherewithal to get things." If this is what we get from our teachers, what can we expect from the pupils? After this I do not think I can possibly be charged with having overstated my case. It is, of course, quite a reasonable thing to say that that would be a drab and cheerless world which had no brightly-dressed shop-windows to please the eye and delight the inveterate shoppers; but this is quite a different proposition.

Economics does not by any means exclude luxuries from the category of things that go to satisfy human desires. Apart from moral and physical considerations that undue luxury, coupled with idleness, tends to physical, mental,

and moral degeneration, ultimately defeating its own ends, there is no reason why man should not enjoy every luxury that Nature in her bounty can be induced to yield in response to human effort. But a sane humanity—provided it had reasonable control of the economic machinery and acted in concert with a common end in view—would obviously take care to so arrange matters that the effort given to the production of luxuries should follow, and not precede, that given to the production of comforts; and that the effort given to the production of comforts should follow, and not precede, that given to the production of necessities, sufficient for all. Just as one poison is an antidote to another poison, it is, under the present chaotic conditions, frequently the case that the wasting of human effort in the making of perfectly useless "frills" is an antidote to the more desperate disease of making nothing at all, for reasons which we shall see more clearly presently. But the mental disease which sees economic salvation in the making of useless "frills" is a legacy of the poisonous Mercantile Theory, for which there is apparently no antidote whatever. That those impregnated with it should be in positions to transmit the disease broadcast is much to be deplored.

Having, as I trust, finally removed the monstrous obstruction from the path of economic conception, we are now prepared to take a comprehensive view of the true forces and mechanism governing the production of utilities.

CHAPTER XII

PRODUCTION AND INCOME—A WITCH'S CAULDRON—
MONEY AND ITS SUBSTITUTES—THE LANDLORD'S IN-
COME: WHAT IT CONSISTS OF—MIDDLEMEN—BANKERS'
CURRENCY—PAPER CURRENCY AT A PREMIUM

ONE of the earliest lessons enforced in the science classroom or primer is that of the limited scope and unreliable nature of human perception, and the narrowness of the untrained mental vision. But I venture to think that in no other science than economics is the cramp on the mental vision fastened with such merciless tenacity, and is so difficult of release. Every environment and incident in a man's life tends to give an extra twist to the vice-like grip. Accustomed to a narrow conception of production as limited to those engaged in agriculture or mining, and in shaping natural materials into usable commodities, he sees a great host of people engaged in occupations which are, in his view, not productive. A little reasoning may, perhaps, convince him that the musician, singer, and actor, are also producers; but to extend that conception to the check-taker at the door would seem to him ridiculous. And yet all these thousands engaged in unproductive occupations get their wants satisfied—some of them prospering exceedingly—all because the occupations command money rewards. What, then, can be more evident than that the money is the talisman which calls things into being, and that wealth means money? To interpret pro-

duction in the sense of utilities of all kinds, to conceive of the economic structure as mankind engaged in rendering services of all degrees of usefulness, given and exchanged by means of some medium recording indebtedness for past services rendered, requires no small amount of mental training, to overcome the inherited and acquired preconceptions. No less a business man than Sir William Lever said some time ago that working men are frequently better served than their employers, insomuch that they get their wages whether their work is productive or unproductive—this of the men employed in his own and other factories, making soap, cottons, woollens, boots, and so on. No doubt by "productive or unproductive" he really meant profitable or unprofitable; but his careless use of the term is exceedingly instructive, as indicating the general conception that men are engaged in money-getting, no matter whether by making useful soap or useless frills. If the employer can see no money profit at the end, the tons of soap, woollens, or boots, become merely the painful evidence of so much labour wasted unproductively!

From the conception of an atom to that of an electron may be a vast stride, but there is nothing virtually more puzzling in the one than in the other, the difference being rather one of degree than of kind. But from the conception of a heterogeneous multitude of humans, each hunting for gold "on his own," to the conception of a world closely and intimately co-operating in the production of utilities for the satisfaction of human desires, where proprietary rights are man-made institutions, and where products are portioned out by means of credit tokens having behind them the force of universal consent, is a transition too startling to be assimilated without protracted mental discipline. Seeing only a very minute portion of the economic mechanism, and that only through a tiny

prismatic ray, it is no easy matter to train the mental vision to see a world-wide structure, intimately interlocked. To the man in the street, the proposition that getting things for money always means a return for services rendered seems to be the most chimerical nonsense. How can that be, one will say, when, as a matter of fact, thousands of men who have rendered no service whatever—who may have won the money at a race-course, a lottery, a gambling den, or even stolen it—do get whatever they want for money? For all that, the money, however obtained, represents credits on productions in return for contribution made to the stream of production. That the social adjustment is so constituted that some do the producing while others have the legal right, the ingenuity, the cunning, or the dishonesty, to become possessed of the credits entitling them to the equivalents of what has been produced by others, does not alter the fact that money commands utilities because it represents utilities already given up for consumption. Someone must first fill the lucky tub before anything can be got out of it. Unless it is constantly being filled, the prize tickets will soon be of no avail. In the effort to get much out of the lucky tub, men are frequently led to contribute much to filling it; and from that point of view the upside-down conception of the process is not wholly a disadvantage. But if the economic process is to be understood, and the best means adopted to remedy its shortcomings and breakdowns, we must learn to see it in its true sequence and wide bearing, not the inverted image seen by the mass of mankind.

I can fancy some of my readers saying: "But are you not paying too much attention to the man in the street? Don't you think that the more advanced section of the nation are growing out of this crude economic conception?"

Well, here is a very recent example. In a newspaper of large circulation there was an article entitled, "The Capitalist and his Millions: A Working Man's Delusion." The following is an extract from it:

"An employer, for instance, may make £1,000 profit. That is duly assessed, taxed, and recorded. Most of the money is immediately passed on to dozens of shopkeepers, merchants, suppliers of various materials, doctors, servants, agents, etc. Many of these are income-tax payers, so portions of the original £1,000 go to make up the profits or incomes of these people, and are reviewed by the revenue officers. The money is passed on, and on and on, and portions of it are assessed again and again."

A, the merchant, spends £100 of his income in groceries which are consumed by himself and family. £10, say, of that £100 appears later as the grocer's profit—a part of his income. "Ah," says the writer, "that £10 is not only part of the grocer's income, but was also part of the merchant's income. It is the same money, and may have already paid income-tax once, twice, thrice, perhaps a hundred times. So it comes to this: that if a nation—Great Britain, for example—produces in the course of the year two thousand millions' worth of goods and services, but only employs one hundred and fifty millions of coin to effect the exchanges, the annual income of the nation is just one hundred and fifty millions, and not two thousand millions! This is obviously too absurd. Of course a man's income is made up of products and services; the money terms merely express their exchange value. If the merchant pays £100 a year in wages to his gardener, he gets £100 worth of services which materialises in part, perhaps, in fruit and vegetables, and in part in the satisfaction and pleasure which he derives from his garden. The gardener has created £100 worth of wealth—I say wealth

deliberately: the pleasure derived is wealth—which is consumed by the merchant, and in return gets claims on the production of others to that value. Allowing that the merchant's income is the reward of services rendered, the £100 in wages paid to the gardener is not £100 worth of wealth counted twice over, but £200 worth of wealth—the £100 worth created by the merchant and the £100 worth created by the gardener. The actual wealth created by the merchant was, or is being, consumed by others. In return he gets the wealth created by the gardener; and the gardener in his turn gets the equivalent in wealth created by other producers. All these are separate incomes—wealth created to provide the incomes—though the coin or paper used to transfer and exchange the wealth may have been used over again in many transactions. But even where a person's income is not a return for services rendered, it is still true that the income is the result of wealth created, and that each income stands for so much wealth added to the general store. This we shall see more clearly as we proceed.

In endeavouring, then, to form a broad mental view of the economic structure as a whole, perhaps the first thing we must thoroughly realise is that men exchange services by means of a vast system of credits. It is no longer a matter of, "I give you this if you give me that," but, "I claim this as the agreed-upon return for services already contributed to production." Each worker of whatever degree and kind gives his quota of service to a gigantic witches' cauldron, fed by a multitude of conduits converging to it from every point of the compass, which, after many mixings and brewings, after numerous changes and metamorphoses, at last emits a vast stream of utilities, ready for consumption. In return he receives certain

counters, checks, or tokens, backed by the legal force of every country and State, intended to secure to him some stipulated quantity of utilities out of the general stream, such as the economic conditions enable him to exact. In effect, the credit instrument, be it of what it may, bears on its face the impress that "the community is indebted to the holder for so much of utilities in return for services rendered to the production of utilities." I said that the credit instrument is "intended" to secure some stipulated quantity. Like all human contrivances, it does not always succeed in its purpose, as we shall see presently.

The production of utilities is dependent upon certain indispensable precedent conditions. To the primary factors of land, labour, and "fixed" capital—the "real savings" of past human labour—there must also be added the necessary factor of "fluid" capital, by which is meant the possession of credits on production, come by as a result of "personal savings" which may or may not have materialised into real savings. To enable the worker to draw from day to day so much of utilities from the stream as his labour will command, either the worker himself or his employer must be holding a certain quantity of claims on production, as a result of past services for which no equivalent had been taken out. These claims, as we have seen, are no sooner given up in exchange for utilities than they start on their way back to the various employers, and are by them redistributed, to be once more given up for utilities—except in so far as they may be "saved." The amount of money or bank credit need, therefore, be no more than will be replaced when the goods are passed by one employer to the employer in the next process, finally reaching the consumer, and continuing the circle once more. Or the banker may loan the necessary credit, pending its replacement by the credit coming from the

employer in the next process ; each credit for goods sold thus replacing the last loaned credit, one deal covering the other and keeping the loan at its original sum, until such time as the prosperity of the business permits of its being reduced or extinguished altogether.

It is the credits on production resulting from personal savings that the art and organisation of banking turns into currency. Substantially the organisation of banking consists in gathering and concentrating the personal savings of many individuals under one control ; and by keeping up a high degree of confidence in their standing and stability, coupled with the fiction—the necessity of which we shall better understand presently—that there is gold awaiting to meet every possible claim, the bankers are able to use their clients' deposits and the legal claims on production represented by securities as money, under the guise of promises to pay in gold. They thus obviate the necessity of employing gold, or other "commodity" money, as the medium of commercial exchange—proceeding that would be utterly impossible in the present magnitude of exchanges, and, if it were possible, would involve a ruinous expense. Many economists prefer to call the bank currency "substitutes for money," as distinct from gold and silver money (according to the "standard" employed in different countries), which they call "real money." Well, those who have read the preliminary chapter "On Definitions" will, I trust, fully agree with me that it matters little what verbal symbols are employed so long as we have clear-cut conceptions of the realities. Since the bank credits do, as an actual fact, perform the function of the medium by which exchanges are effected, they do just what "commodity" money did, and would be required to do, in absence of the bankers' money. The term "currency" has also the technical meaning of an instrument of exchange

which passes current without question from hand to hand, the same as the Bank of England note, or the legally established paper money in various countries. But though the cheque does not pass current exactly in that way, I am satisfied that there is nothing to be gained by the classification into real money and substitutes for money, or by paper money which runs current and that which does not quite run current, though it most efficiently performs the bulk of the money function. The fact that the cheque has taken the place of the bank-note is the mere accident of a legal monopoly secured by the Bank of England, in the belief that they would thereby secure the bulk of the banking business. But for this, bank-notes for denominations from £1 upwards would now be circulating largely, which would pass current from hand to hand ; and it was to defeat the Bank of England monopoly of note issue that the use of the cheque had developed to its present gigantic dimensions. If I may paraphrase a popular maxim, I would say that "money is as money does." At any rate, we have the conceptions clearly before us ; and I can see no room for misinterpreting the process, owing to our use of misleading terms. On the contrary, the misleading terms are wholly on the side of the "real money" school, and the entire statement of the economic problem in terms of money, which is in no small measure responsible for the baneful persistence of the mercantile theory.

We shall more effectively visualise the economic process under consideration if we now present it in several concrete illustrations, instead of in general terms. Let us begin with the most important of all productions—the farming and allied industries. The farming industry in this country pays in round figures some £35,000,000 per annum in rent, and retains in what is called profits just about half

the sum. Now, though the farmer consumes some small part of his own produce, yet, since all but a small fraction is sold in the market, it will be more convenient to conceive of the industry as contributing wholly to the general stream of production. As each of the farmers, market-gardeners, breeders of horses, sheep, cattle, pigs, and poultry, providers of milk, butter, and eggs, hands his products to the one engaged in the next process, he receives from him certain forms of claim, constituting credits on production. Part of these he has to distribute amongst his labourers and those who have co-operated with him in providing tools, machinery, farm buildings, or artificial manure; and, of that which remains, two-thirds of the claims must be handed to the landlord by way of rent. Now, though the landlord, *qua* rent-receiver, is a non-producer, yet the claims which he holds on production represent contributions to the stream of production.

Let us now suppose that a number of these landlords save part of their rent rolls. We will first assume that they invest their savings in some municipal securities. The loans are employed, let us say, in the construction of roads, bridges, electricity and gas works, waterworks, and similar public services. Or perhaps they invest in a railway undertaking, a telephone service, a tramway service, or the construction of docks. Now, what is it that actually takes place? Why, it means that the farmers, market-gardeners, breeders, and others, tenants of these investing landlords, are contributing to the stream the products which are being consumed by the workers on the undertaking in which the investment is made—or the equivalent of these products after being exchanged for other utilities. The claims on production received as rent are transferred, in the form of bank credits, to the municipal authority concerned. The actual coin employed in the process is

probably very little more than the weekly wages bill, circulating between consumers and banks week by week. It means further that the farmer's productive efficiency must be such that there is a surplus left over for the maintenance of the workers on the undertaking in question, to the extent of the investments, as well as the maintenance of their landlords. It means further that the "personal savings" of these investors have now materialised into "real savings." And last, but by no means least, it means that "fixed" capital has been created, by means of which human capacity to produce wealth will be greatly increased, out of which a certain share will go as interest to the investors or their heirs.

Let us now suppose that they have invested in a war loan. The agricultural products of the farmers will now go to feed the soldiers; the leather made out of the hides of the cattle will go to make them boots; the wool from the sheep to provide them with clothing; or it may be that these things will be consumed by the workers engaged in making ammunition, gunpowder, and other explosive materials used in the war. The "personal savings" will remain, in the form of Government stock, pledging the future production of the nation for the payment of annual interest; but no "real saving" has been made. Nothing is added to the fixed capital which would make production more plentiful. With the indirect and far-off consequences of war-making and conquests we are not in a position to deal. But taking the case of wars between nations somewhere about equally advanced in civilisation and economic progress, it may be taken as axiomatic that, no matter which of the combatants proves to be the victor, there is no prospective economic gain, but that, on the contrary, both the nations and the world at large are impoverished thereby for many years. A great quantity of wealth is actually

destroyed. The stream of production is drawn upon to its utmost capacity for the maintenance of, not alone of the regular army and navy, the reserves called away from productive occupations, and the motley horde of army followers and hangers-on, but also for the maintenance of a multitude of workers who are withdrawn from the production of things for the preservation of life, and are set to produce weapons, engines, and materials, for the destruction of life and wealth. In addition to this, the economic machine, so largely dependent on international credit and banking, becomes disorganised and demoralised, causing many business failures, and arresting production in many parts of the world. This quickly brings about a shortage of necessities in the stream of production, with the resulting phenomenon of a rise in prices, which diminishes consumption, entailing much suffering, and bringing many to the verge of, if not to actual, starvation.

Let us now suppose that the investment is made in some industrial joint stock undertaking—say the building, equipping, and carrying on the industry of a boot factory. Here we must revert briefly to what has been said as to the nature of securities. The claims created by securities are of an entirely different nature from the money claims for services rendered to production. If the tailor sells a suit of clothes for £5, whether he is paid in cash or by cheque, he expects to get some definite quantity of other utilities which he knows by experience to be procurable for that sum. But if he invests the £5 in a public security bearing interest at 3 per cent., he has in fact relinquished the claim on production to that amount, in return for which he acquires the right, guaranteed by Government or municipality as the case may be, for an annual claim on production to the value represented by 3s. He can sell his security, if there is a buyer, for a capital sum, but that

only means that someone else has relinquished his capital claim. In the case of investments in ordinary joint stock undertakings, there are many legal devices and complications for creating priorities to the various holders. Thus, there may be debentures, first, second, and third preference shares at stipulated interests, with perhaps, conditions as to sharing profit also, and ordinary shares; but these complications are not germane to our point. The investor in such an undertaking gives up his claim on production in return for a legal contract to share in the profit of the business. If it should turn out that there has been a miscalculation, that the supply is already ample to meet the demand, and the business should entirely fail, the investor loses his personal saving, and there is also no "real" saving in existence, so long as the building and plant remains out of use—a "derelict" on the wide industrial ocean. The community is the poorer by so much of human labour expended to no purpose, which might have been employed either in the production of "real" capital or of consumable utilities.

We will now suppose that the landlord's personal savings are deposited in banks. Banking, as we know, is not the same thing as "safe deposit" business. A deposit at a bank is a loan to the bank, against whom there is only a legal claim for repayment, according to agreement. Here is where the banking organisation steps in, creating a currency of their own—the "fluid" capital necessary to industry—on the strength of the credit and securities deposited by their clients. With the exception of small retail purchases, the practice of buying and selling on credit is now practically universal. The wide distances frequently separating buyer and seller, the time that must elapse between purchase and arrival of goods, and between arrival and sale, and many other evident reasons, have

tended to establish this universal custom. These reasons are, nevertheless, what we should call the immediate causes, as distinct from the ultimate cause. The ultimate cause lies in this: that but for the credit system production could not have come to within approachable distance of its present dimensions, so that the cause and effect are, in a sense, reversed—or, at any rate, they react on each other. Just as the existence of a commodity currency made division of labour at all possible, the gradual evolution of the credit system made possible an immensely more minute and elaborate subdivision, and with that a much greater productive efficiency.

Take one or two examples. Of the many Bradford cloth manufacturers, each lays down a number of designs and qualities for a particular season's trade. The tailor in London, Birmingham, Manchester, or Bristol, requires, however, convenient access to, and ready choice of, as many designs and qualities as possible. Manifestly, it is more convenient for him to deal with a factor who makes it his business to stock the goods of many manufacturers; and still more so is it to the convenience of the manufacturer to deal with two or three factors, rather than send out a host of travellers to solicit small orders from the many tailors all over the country. Labour is thus economised, and the price paid by the tailor is no more, or perhaps even less, than he would have had to pay if each manufacturer had to send out travellers to call on the retail trade. Or take the case of the general drapery trade. The stock contained in the average drapery store represents the turn-out of a very large number of manufacturers, spread all over the country and abroad. The small or moderate buyer finds it decidedly more convenient to deal with a wholesale house, and the manufacturers find it to their interest to give the wholesale houses special terms.

When to this is added the system of credit, the manufacturer is obviously in a worse position for giving credit to a large number of small buyers all over the country than the wholesale factor who lays himself out for this kind of trade, and whose connection is, perhaps, largely local. As a matter of fact, however, many of these divisions between maker, middleman, and retailer, have become considerably obliterated during recent years, with the concentration of retail trading into fewer hands, conducted on a large scale. In the minds of most people, the middleman is a mere interloper, who squeezes himself into an industry where his services could readily be dispensed with, causing an increase in prices so that he may make a profit. In the main, however, the middlemen are an integral part in the economy of production as organised at the present day, though some of them are, indeed, a sheer excrescence on the economic structure, whose existence is an unmistakable symptom of organic and functional disease. This point we shall have to consider further at a later stage.

Now, it requires no superabundance of imagination to realise that, were all these complicated transactions and exchanges carried out by means of spot cash, the quantity of coin required would be staggering beyond description. We can take the bank clearings as some rough indication. I see that last year (1912) they amounted to sixteen thousand millions (£16,000,000,000). If we allow for the time elapsing in wholesale trading between the purchase and delivery of goods, and between delivery and sale, we cannot assume anything more rapid than a monthly turnover. When to the recorded bank clearings is added the other clearings referred to in a previous chapter, it means that the quantity of coin that would have to be stocked (apart from retail purchases, where the turnover is much

more rapid) for the commercial dealings carried on by the people of this country alone could be nothing less than two thousand millions sterling (£2,000,000,000). What it would mean for the whole world I cannot pretend to guess. Scarcity of gold—supposing that gold remained the standard coin under such conditions—would, of course, raise its commodity value, and for the purpose of coin it would have to be much cut down in size. But even if cut down to the merest handling capacity, and supposing that there is within the bowels of the earth sufficient gold for such requirements, it would necessitate the employment of very many hundreds of thousands of additional workers for extracting and preparing the gold. To the one who conceives the economic structure in terms of the mercantile theory (his name is Legion) all this would be clear gain, since it would provide so much additional employment. What it would mean in reality is, that the workers who are employed in producing the necessary utilities would be saddled with providing sustenance and comforts for a huge army of gold-diggers, refiners, assayers, minters, transporters, employing exploiters, tool and machine makers, etc., whose labour is now free to be employed in creating consumable utilities to add to the common stock. It would mean further that, before anyone could set out in organising a conscious co-operation of labour in some unit of industry, he would first have to accumulate a hoard of gold—as a result of the products of past labour given to be consumed by the gold-producers—for performing the function of the exchange medium necessary for the volume of his trading turn-over. Fortunately for mankind, gold was not obtainable in such abundance, spite of the most heroic efforts. And so, after numberless attempts and many disastrous failures, mankind has succeeded in organising a credit currency, only just tolerably efficient

to meet the productive capacity made increasingly fruitful by scientific invention, organising ability, and the amalgamation of the habitable earth into one economic unit. To the critical reader, the question will no doubt occur, Could not the present use of coin be further minimised, or entirely dispensed with, thus liberating more human effort for the production of those utilities of which many are going short? This question will be reached in due course.

With the modern development of banking, much of the complexity of the credit medium of bills of exchange has gradually come to be simplified and made more efficient. Bankers are in the best possible position for forming a sound judgment of the financial standing of their customers. In most cases the customers keep current accounts, which they do not allow to fall below a certain margin; and these form convenient securities against discounted bills in the event of their being "dishonoured." Many of their customers hold public securities, on which the banks are prepared to make advances on terms not readily obtainable elsewhere; and even when the securities are deposited only for safe-keeping, they form a fairly reliable guide to the customer's financial position. Apart from these, the banks can generally tell from a customer's turn-over and the condition of his account how far he can be trusted with reasonable safety. Instead, therefore, of a bill having to be transferred from hand to hand, the credit in each individual case depending on the strength of personal standing and reputation, the bank converts the bill into banking credit, thus making it, in effect, an impersonal credit. A, who holds a bill on C, instead of offering it to B as security against the purchase of goods on credit, takes the bill to his bankers, who give him a credit on their books. He has now no need to ask B for credit; though, in actual fact, all that happens is that, instead of offering

to transfer to him a credit on C, which would necessitate B entering into an anxious mental calculation as to whether the double security of C plus A is sufficient to justify him parting with the goods. A transfers to him so much of the bank credit, which is at once accepted without question or demur. B may then, by means of a cheque, transfer the credit to D, D to E, and so on, until finally C, by a transfer of credit from his bankers to the account of A, in payment of the bill, completes the series, the whole circle having thus effected their exchanges without the intervention of a coin. The stability of the banks being taken as a matter of course, each accepts the bank credit as currency, just as one accepts a bank-note, a dollar bill, a rouble, or any other established paper currency.

In the course of modern industrial enterprise amongst advanced nations, with trading credits running into big figures, the need to take advantage of fluctuating market conditions, a large influx of orders at one time and a corresponding slackness at others—to say nothing of spasmodic speculative dealings on a large scale—even those who start with an ample fluid capital at command find themselves frequently, in the intervals between buying and selling, short of the requisite currency. Many others, eminently capable of organising and conducting industrial operations, are without that amount of fluid capital necessary to start business successfully. Subject to such precautionary measures, and on the strength of such security as experience has taught them to be necessary, the banks utilise the credits on production lent to them by their customers to re-lend at interest, thus creating the currency which sets the wheels of production in motion. Once more, then, the claims on production saved by the landlords in question, as a result of their tenants having contributed products to the general stream of production, are utilised for setting a

number of people to produce more wealth. By means of these claims, or credits, the creators of the fresh wealth are able to draw from the stream, from day to day, those utilities necessary for their maintenance, emerging therefrom as a result of the co-operation of labour of all kinds, manual, mental, and organising skill, during yesterday and many days before that; and in their turn they are creating the utilities to-day which will emerge to-morrow and many days after for the maintenance of those who will then go on creating fresh wealth. No amount of claims—no sort of money—will avail to keep production going beyond the provision of consumable utilities available for the sustenance of those who labour to produce wealth. Gold will not cure a famine; the food for making good the shortage in one district must be created by human hands and brains in other districts. It is true that a contribution of gold in relief of a famine, whether from the national exchequer out of taxation or by voluntary subscription, has the indirect effect of leading many to economise in their consumption, thus leaving a greater “surplus” available for the sufferers from famine; but this indirect effect is produced equally by a contribution of credit-currency. The greater the number of those who consume without contributing anything to production, the greater must be the productive capacity of those who are engaged in producing. The shortage, and the maintenance of non-producers, can only be made good out of “surplus wealth” created by others. It does not follow that any part of the personal savings has materialised into real savings, but in the course of industrial enterprise it is almost certain that some part of it will have been turned into fixed capital.

Let us now suppose that one of these landlords expends the whole of his income; and, for the elucidation of the

point we have now to consider, we will suppose that income to be more than ordinarily large. The size of his income is expressed by the amount of money or credits that he receives in rent; but that, in turn, depends upon the quantity of agricultural products contributed by his tenants to the stream of production, and made available for the consumption of others. In return for that contribution, they receive claims on production in general, part of which they give up to their landlord as rent.

The landlord thus becomes entitled to draw from the stream of production to the equivalent of the claims transferred to him by way of rent. But however big the claim, he cannot draw from it that which it does not contain—it must first be put there before it can be taken out. We may suppose that his particular tastes in the way of expenditure consist in entertaining a large circle of friends at table; in keeping up a large retinue of servants; and a racing stud with the necessary paraphernalia of trainers, grooms, stablemen, etc. Conceivably, all but a relatively small part of the things demanded by him may consist of the very products contributed to the stream by his own tenants: the food for himself, his guests, servants, and horses; the wool which is turned into clothing for their wear; and the hides which are turned into leather for their boots and saddles. We say that it is his income which provides for the entertainment of his friends, and for the maintenance of his large retinue, his horses in their stables, and his dogs in their kennels. Just so, insomuch as the legal claims on production are his by social consent. But the student of economics must never allow the mental vision to become obscured to the fact that what actually provides for the maintenance of these non-producers is the "surplus wealth" created by the tenants on this particular estate.

We will now suppose that his principal taste in expenditure runs into diamonds and other precious stones, expensive wines, silks, and other rare luxuries, all imported from abroad. Here at least, one will say, it is money which procures the luxuries. Well, in very rare cases it does indeed happen that imports are paid for in gold, which never comes back. But, as has already been explained, the proportion of payments for imports in gold is very tiny; and against that we receive as much or more gold, on the average, in payments of exports. What it really amounts to is that, like the circulation of money in the home trade, the gold merely performs a circle; but behind the gold is the exchange of goods for goods. I suppose it will be almost a shock to the reader to be told that in many Continental centres paper money stands at a premium. If you go to a banker in Italy to change your English money for the currency of the country, you will get a slightly better rate of exchange for paper—bank-notes, banker's draft, or even a private cheque if the name is well known—than you will for English gold. The reason simply is that the banker has no use for the gold, and it only has to go back to London, involving cost of carriage and insurance, whereas the paper can go in an envelope for a penny stamp. Once more, then, it is the products put into the stream by the tenants which are used for the maintenance of the workers engaged in mining the diamonds, attending the vineyards, or weaving the rare silks. It does not follow, indeed, that these workers live on the very identical beef, potatoes, and cabbages put into the stream by the tenants in question. It requires no great stretch of imagination to picture the beef, potatoes, and cabbages consumed by workmen in Yorkshire and Lancashire, who are thereby made fit to produce cotton and woollen goods; that these goods go to Natal to be

worn by labourers on the farms there, who are thereby made fit to produce another lot of beef, potatoes, and cabbages ; and that the workers in the diamond-mines consume the beef, potatoes, and cabbages, produced on the Natal farms, and are thus made fit to work the diamond-mines. In effect, then, it is the beef, etc., created by the tenants under consideration, which is the direct cause of creating a similar supply elsewhere, used for consumption by the producers of the luxuries.

The picture is only out of focus in matter of time. It will be more in conformity with actuality if stated in this wise : The beef, etc., grown by the tenants in question two years before, went to feed a number of workers employed, say, in building a steamship. The steamer was subsequently employed in carrying cotton goods to India. The producers of the cotton goods, as also the owners of the ship, exchanged their goods and services for Indian silk and tea. The cotton goods are worn by Indian agriculturists, who produce the requisite food for the maintenance of the silk and tea workers. The silk is then consumed by the landlord, and the tea is consumed by the workers on his tenants' farms, both having become entitled to these products in return for having contributed the food for the maintenance of certain workers who, through a long chain of exchanges, enable the production of other food in India for consumption by the silk-weavers and workers on the tea-plantations. The essential point in this more nearly adjusted focus (an accurate focussing would scarcely be possible) is the vast system of credits on commodities and services in return for services rendered, and in many cases consumed long since. Every child is born into the world with a tremendous load of debt hanging over him. Some of it has been contracted by the Government of his country, and payment will be exacted from him, in the

form of taxes, without any return whatever. For the rest, everything he is destined to produce, and every service he will render, is already pledged as a return for services rendered and consumed ; but in so far as the economic forces will enable him to do so, he will, in his turn, get a credit on future production. He is paying a debt contracted by others in the past, and in return gets a credit on the production of others, present and future. It is the only system on which production on any but the most primitive and abject scale is at all possible. It has grown out of the necessity inherent in co-operative production, where a large number of people contribute to shaping a natural gift into a consumable product. It works more or less satisfactorily (apart from equitable apportionment) so long as the credit instrument does not get out of order. When by tampering, wrong notions, or bad management, the credit medium is deranged, partially ceasing to function, it spreads ruin far and wide. But of this anon.

It matters not if, in place of the rent being derived from agricultural land, it comes from urban sites. The occupiers of the factories, shops, or dwelling-houses, create surplus wealth, which they exchange for general claims on production, part of which is given to the landlord as rent ; and though it may be that the particular form of wealth created by those urban tenants is not such as is in demand by those who produce the goods which are sent to South Africa in exchange for the diamonds, yet it remains literally true that these workers are maintained on the surplus wealth created by the urban tenants in question. If the workers' demands chiefly consist of foodstuffs, while the wealth created by the urban tenants consists wholly of manufactured goods, it will result in these goods being sent to Canada, Argentina, Russia, Denmark, and many other places, and there exchanged for the foodstuffs

required by the workers on the goods which are sent to South Africa to be exchanged for diamonds to satisfy the desire of the landlord. And all this is accomplished by means of effective demand. The landlord, who holds an undeniable call on products—come by as a result of contributions to the stream of production—demands diamonds; the workers in the diamond-mines demand cutlery and beads; the producers of the cutlery and beads demand foodstuffs; the growers of the foodstuffs in Canada, Argentina, and so on, demand machinery, boots, and other manufactured goods; and these latter are drawn from the contributions to the stream of production made by the urban tenants of the landlord who demands the diamonds. The diamonds come into being as a result of the products contributed to the stream, on which the landlord holds a claim, which are used, in however roundabout a way, to satisfy the actual desires of the diamond-producers. In actual fact, the mechanism is immensely more complex than this; and it is because of this complexity that so many of us find it difficult to form a clear mental grasp of the process, and only see an inverted image of a money talisman calling things into being by its magical properties.

How the economic force which we call "effective demand" operates; how it causes a flow of luxuries into the stream though there is a shortage of necessities; how it brings into the stream many monstrosities pandering to vice and crime: will be dealt with in greater detail in the next chapter. But perhaps a few words should be said here to dispel any notion that may arise in the minds of some of my readers that I have purposely designed to hold up the landlord as the archetype non-producer, consuming in idle and ostentatious luxury the wealth created by his tenants. There are, of course, as we all know, many other ways in our economic system of

deriving large incomes without contributing anything to production, and of receiving much greater incomes than is warranted by productive efficiency as distinct from the artificially-created exclusive access to superior fertility. Nor does it follow that, though *qua* rent-receiver he is a non-producer, a landlord may not, nevertheless, voluntarily render important services to the nation, as many of them are doing. Neither am I intending to suggest as a fact that those who derive incomes from rent of land are, as a class, more prone to ostentatious luxury than those who derive their great incomes from industrial sources. The choice is convenient for purposes of illustration, because the landlord stands out so readily as a clear type of non-producer, and, generally, as one deriving a handsome income from wealth created by others. His ethical right to that income is not the point at issue, since we are engaged in an economic investigation, and not in a study of ethics.

CHAPTER XIII

PRODUCTION AND SOCIAL NEEDS—LAW OF “EFFECTIVE” DEMAND—PERIODIC SLUMPS AND BOOMS: THE THREE CAUSES—“OVER-PRODUCTION” AND “UNDER-CONSUMPTION”—PRODUCTION OF LUXURIES DIMINISHES PRODUCTION OF NECESSARIES—STARTLING EFFECT OF HOARDING—“USELESS FRILLS” AS PALLIATIVES TO ECONOMIC DISEASE

ONE of the black spots—if not the blackest—of production as developed at the present day is the fact that there is no intelligent adjustment between production and social needs. Not only is there no rational plan in the choice of things to be produced, based on some conception of a graduated scale of necessity and usefulness, but even in the production of those things which are of admitted necessity and usefulness, the economic forces operating in regulating production are of a crude, uncertain, and haphazard character, resulting at best in periodic slumps and crises, entailing misery and suffering from which even the fairly prosperous do not escape. One does not expect from fallibility a perfect sense of prevision, nor yet a keen regard for posterity from the ethically lukewarm. But the point is that, under present conditions, not only is there no sort of conscious effort or attempt to adjust production to social needs, *because of social needs*, but even such indirect forces as tend to redress the balance are altogether inadequate, and are largely made nugatory by the social

conditions. Under conditions not far removed from “freedom of access,” and before machinery and “industrialism” have entirely revolutionised the system of production, the disparity between production and needs could not become very pronounced. Then, as now, the discoverer, *e.g.*, of the far-off and not easily accessible coast-line where pretty shells could be gathered cared nothing if some of those who bartered necessities for his shells themselves went short of necessities in their passion for ornament. Here and there people will deny themselves common necessities rather than go without finery. But as a general rule the provider of ornaments and finery will not prosper where the disparity between incomes is small and the supply of necessities little more than sufficient to meet the recognised standard of needs. If game is plentiful and the soil fertile, the providers of finery will prosper and increase in numbers; not because—it is perhaps necessary to enforce yet again—of an abundance of money, but because the capacity of those engaged in producing the things needed to sustain life and health is such that a surplus is left over for the maintenance of those engaged in collecting shells or in making other articles of finery.

With the private ownership of land and consequent derivation of income from rent; with the accumulation of the implements of industry—fixed and fluid capital—in few hands, and the consequent derivation of income from exclusive access to capital (the “rent” of exclusive access as distinct from, and in addition to, personal effort and efficiency); with the vast disparity between the riches of the few and the poverty of the many; with the firm establishment of a currency operating as an admitted claim on production, and presenting an inverted image of the economic process: the adjustment of production to

needs becomes dependent upon an economic law which operates indirectly and spasmodically, entailing much waste and hardship, which, if not entirely avoidable under any conceivable conditions, could nevertheless be reduced to a minimum, and which would scarcely be tolerated if the causes operating were fully understood and realised.

The law operating is that which is known as "effective" demand. Mere demand—*i.e.*, the fact that many people are wanting the thing—is of no consequence; it must be the effective demand of those who have something which is also in demand to give in exchange for the thing demanded. It must not, however, be imagined for a moment that demand necessarily precedes supply, or that there is, indeed, any sort of order or sequence between the two. In a rough—a very rough—way there is, in the long run, an approximation between the two, operating through price, as has been explained. But in most, if not in absolutely all, cases the action is that of a wave of greater or less magnitude, which rises and falls periodically, spasmodically and feverishly adding to its volume where effective demand tends to increase for some time, and gradually but intermittently diminishing in volume as the demand tends to slacken from some cause. Even in the case of many of the staple foodstuffs the wave is well marked, rising to a crest and falling into a trough in almost regular periodic succession. Thousands of people are engaged in producing something for which they merely hope to create a demand, in which they sometimes succeed, but more often fail.

In the first place, then, let us endeavour to get a clearer insight into the operations of supply and demand. As it happens, the production of diamonds is practically a complete monopoly, and so stands on a different footing

from production in general. We want to know rather how production is governed in the case of more or less staple commodities produced "in open competition"—a term which must, however, be understood as having only a relative significance, since the "exclusive access" of capital and organising ability gives more or less of monopoly to all industries of any pretensions. An absolutely accurate adjustment of supply to demand is, of course, beyond human control, even if all the conditions of demand were known, owing to the natural variations in the yield of agricultural products and the raw materials of industry. But even if there were no such variations, the very conception of an exact balance between supply and demand is utterly futile, since demand itself is a shifting quantity depending upon two main factors. The demand for a given commodity will depend (a) upon its price—*i.e.*, its exchange ratio for other commodities—and (b) the general prosperity of the potential buyers—*i.e.*, their increasing capacity for producing other wealth to give in exchange for the thing demanded—to say nothing of accidental causes, such as change of fashion, acquired habits, etc. But the price itself is, again, dependent upon two factors. It may fall through greater economy in production—*i.e.*, when by means of better tools, machinery, or organisation the same labour will produce a greater quantity, so that the effort expended in the production becomes less in relation to the product for which it is exchanged in which the labour effort remains as before—or the price may fall, though the cost is not lessened, when there is an undue increase in production. Conversely, the price may increase when through some cause—war, fire, or other misfortune—machinery has been destroyed and organisation broken up, so that production for labour effort is decreased; or when, through commercial crisis or other

causes, less is being produced. The immediate governing cause of price is, indeed, always the quantity on supply in relation to demand ; but the ultimate and prevailing cause is, nevertheless, the labour effort expended in the production (modified by the law of "exclusive access"). While, then, it is not possible to accurately adjust supply to demand for any lengthy period in advance, it is, nevertheless, no very difficult matter to form approximate and fairly reliable estimates of demand for short periods, say from year to year, based on statistics of consumption, allowance being made, of course, for the estimated increase of population. If, in the very attempt to provide a sufficient supply, methods are found for cheapening production, that would not seriously tend to an excess of production, since the lower price would result in a corresponding increase of demand.

In a very rough way the probable demand based on previous records of consumption does actuate the springs of supply. A rise in the price, for instance, of some particular farm product makes it evident to the merchant that, relatively to the preceding season, there has been either a shortage of supply or an increase of demand, or both. A shortage or increase of actual supply is generally fairly well known to the merchant community engaged in a given trade—say, on the corn exchanges of the various capitals, through whom the information tolerably well percolates throughout the trade. But the rise in demand is not so easy to trace. The resources of young countries are gradually being developed—more or less rapidly, as the case may be—and in proportion as the productive capacity of the country, and with that, perhaps, the incomes of the masses, are being increased, products which were previously beyond the means of the great bulk of the peoples of those countries now become

accessible to them. A family may have been content to eat rye bread because the additional cost of wheaten bread was more than it could afford. It is not that they wanted wheaten bread less, but that the difference in the cost between brown and white bread could be expended on something which the family wanted more. But with an addition to the income (in the actual economic fact, additional products available for being exchanged for the utilities rendered by other producers) which leaves something over after the family had provided itself with that thing which it wanted more, the desire for the white bread now becomes greater than a desire for some other additional comfort or luxury on which the added income might be expended. The result is an increase in the general demand for wheaten bread, cakes, pastry, and so on, more or less gradual and pronounced according as the resources of the several countries are being slowly or rapidly developed.

But though in a general way merchants are actuated in placing their orders, and farmers are actuated in the choice of their crops by the possible demand of the coming season, based on the consumption—or, rather, the prices—of the preceding season ; yet this calculation is not collective, concerted, or systematic, but individual and spasmodic, each playing for his own hand with no knowledge whatever of what the other players are doing, with no possible check against the high probability that in the multiplicity of isolated individual efforts to meet an expected demand the supply will overtake the demand at remunerative prices. In the actual result what can rationally be anticipated to happen is what, in fact, does happen. There are three distinct wave-movements in the economic sequence, each of which can be relied upon to happen with almost the certainty and regularity of the

succession of the seasons, or of day being followed by night.

(a) There is, in the first place, the regular annual wave in the case of seasonal farm produce—*i.e.*, produce other than, *e.g.*, fruit, which requires a number of years to mature, and in which the supply is, apart from ordinary variations in the weather conditions, largely dependent upon somewhat obscure causes and contingencies. A brief example will readily make clear the cause of the periodic fluctuation. In Brazil, for instance, the cultivation of rice exhibits an almost unbroken yearly wave, varying to some extent from district to district, rising and falling with the regularity of the tides. Owing to various causes, weather conditions amongst them, some years are bound to be more prolific than others; while the demand on the supply of one district is also not infrequently influenced by the abundance or shortage in other districts. A season of high prices, coupled with an average or more than average crop in a particular district, has the unfailing effect of more land being put to the cultivation of rice in the following season. Not alone are the farmers influenced by the successful year, but an army of merchant buyers are pressing to buy in advance, thus inducing the farmers to strain every nerve to produce a large crop of rice. The inevitable result follows. The unduly increased supply runs down the price, many of the merchants come a cropper, no advance buyers are forthcoming for the subsequent season's crop, and many of the farmers who produced on their own initiative find themselves sadly hit. The result is that many of them forswear rice-growing, and put their land to other crops. What may rationally be expected happens, of course, yet again. With the shortage of supply the price rises, and those farmers who withheld the panic, or were merely too indolent to change a habit,

find themselves well rewarded. As sure as summer follows spring, the rush to grow more rice sets in once again; and so the succession from crest to trough and back again to crest follows in almost unbroken sequence. Except, perhaps, in the case of some few products for which the demand is progressively increasing and the supply of which is not capable of a sudden and large increase, this phenomenon is exhibited by practically all seasonal products whatsoever in a greater or less degree.

(b) In the case of most manufactured goods, the wave is both larger and of longer duration. There the mere fact of a prosperous year, or several years, acting as the psychological factor which we have just been considering, is largely complicated by the conditions of the industry, and by the third wave which we shall examine presently. In the great bulk of the manufacturing trades modern requirements make production on a large scale the condition precedent to success. Let us take some concrete example—say the High Wycombe chair-making industry. To compete successfully with the richer firms, the newcomer and small capitalist, however clever and energetic, must erect a certain minimum of machinery-plant, without which he cannot hope to make his way. There are several engineering firms who are ready to put up the machinery on credit, costing, I believe, between £600 and £700, charging an annual interest on the outstanding balance. But it is in the nature of production by machinery that unless it is kept going full pelt the expense is run up, and if kept going only half-time it is no cheaper, or perhaps even dearer, than sending out the various parts to be cut by the machine sawyers or millers, and doing the rest of the machine-work by hand. As they put it, the machine eats its head off. The engine must be kept going; certain skilled workmen must be kept to

attend to the engine, the cutting, planing, bevelling, moulding, and so on, whether the machine is working all the time or only on and off ; and the interest must be paid just the same. Not only that, but in order to economise, the manufacturer must turn out many of each pattern. To design a new pattern naturally requires time and ingenuity ; and there is also a certain amount of waste before one discovers the most economical way of marking out the plank, batten, or board, for cutting up into the various parts necessary for the chair or settee. There is an essential, indeed an all-important, difference in this respect between hand production and machinery production. The producer on a large scale in a hand industry, so long as a profit is made on the goods, must, as a matter of mere arithmetic, make a bigger income than a producer on a small scale ; but the difference need be no more than in arithmetical proportion. The man who employs only a few "hands" and turns out one hundred units in a given time will, other conditions as to ability to find buyers and so on being equal, make just half the income for that time of the man who turns out two hundred units for the same time. But in the case of producing by machinery, owing to the conditions above explained, the man who produces two hundred units may make a handsome income, while the man who produces no more than one hundred units may make a mere pittance or no income at all. Hence the frantic efforts to produce on a large scale. Indeed, day by day, in all but the artistic individual products, production (I include in that "distribution," as the reader should know by now) on a large scale is becoming more and more a *sine qua non* to any income at all other than from a wage or salary. When a particular trade is prosperous, new-comers will flock into it, all doing their utmost to produce on a large scale. In times of general prosperity,

all industries—perhaps the distributing trades absorbing more than a fair proportion—are taken up with avidity. Further, modern machinery is in the main of a highly specialised character, each being designed to turn out some particular section or part of a commodity, and is practically not adaptable to any other purpose. One machine does nothing else than stamp out the uppers or soles of boots, and another does the sewing ; each standardised part of a bicycle or motor, each ring and bolt even, is stamped out by a separate machine ; and so on. The result obviously is that, if the work is to be remunerative, the turn-out must be on a large scale ; and as the capital employed is of necessity very considerable, and is not capable of being diverted to other employments, the work must be continuous for a lengthy period to recoup the capital expenditure. You have only to multiply a thousand-fold, or many thousand-fold, the concrete examples we have just been considering, to realise what the result must be in a few years.

Well, you will say, the result must necessarily be an enormous, indeed a frightful, state of over-production in the course of a few years. But just think the matter out a little more carefully. We are supposing a time of general prosperity, and all industries, trades, undertakings, and enterprises being taken up eagerly, each accelerating its production with the greatest possible speed. Translate this into tangible terms of the reality—never mind about big profits, large dividends, high interest, and so forth. What is the reality behind such terms ? In plain words, it means that an immensely greater number of things are being produced—this is what you must mean by all producing on a large scale, by "over-production"—you cannot mean anything else. Very well. For every suit of clothes produced before this boom we

are contemplating there are now, say, six suits being produced; for every pair of boots or socks, for every hat, pants, vest, shirt, and hundreds of other things, six are produced now. For every potato grown six are grown now, for every bushel of corn there are now six bushels, and so forth. You can, if you like, leave out a few trades as not being within the circle of this boom; but at any rate it applies to the bulk of production, or it could not be called general over-production. Remember that the conditions we have been reviewing make production on a large scale necessary to minimise cost; that by minimising cost we mean, and can only mean, producing more by no greater effort than it previously took to produce less. We see it very plainly in the example we have chosen for illustration, where for the same day's work the man plus the machine can produce much more in proportion by keeping the machine going all the time. We mean by that, therefore, that with the aid of machinery man's capacity to produce becomes vastly more prolific. We mean that there are more things—or more at any rate of a very large number of things—than there were available for consumption previously. And now think for another moment of what by now we know thoroughly of the meaning of buying and selling. It is an exchange of things and services. The more things there are in being the more we have to give in exchange, and the more those with whom we exchange can give us. In short, there are more things to go round. In what sense, then, do you use the term "over-production"? Of course you do not mean that users cannot be found for the suits and hats, boots and shirts—you cannot mean that.

It can only mean that, though there is any amount of demand—there always is—there is no "effective" demand. But why so? More of nearly everything has been pro-

duced, and since effective demand means the ability to give something in exchange for the thing demanded, how is it that the effective demand has not increased proportionately to the increased volume of the things produced? If at a given time a given number of people have each one unit of something to exchange with the others, and at a subsequent time they have "between them" what is equal to six units each, why not exchange the six units one with the other, and so all have more of what they want to consume—six times as much? Ah, the answer lies in the "between them." There are now six units for every producer to every previous one, if you merely count heads, but the vast majority of the owners of the heads cannot lay claim to the six units of product. They still own one unit each, or very little more, while the other few heads own the rest. The former are not, therefore, "effective" demanders; while the latter, effective demanders indeed, have no desire to consume the things offered—they have had enough. It is not yet fashionable in the City to wear six hats on the top of each other, telescope fashion; and six suits of clothes one over the other would certainly be most oppressive in the summer. Indeed, many of these effective demanders are the very people who hold the things on offer to supply. They cannot dispose of them to those who need them, not being "effective" demanders—perhaps the very men who have made the very things now being vainly offered for sale, while they have to go without. We shall have to revert presently to this economic paradox, after we have considered the third wave, which, amalgamating with the second wave, assumes formidable proportions at regular successive periods, and in its breaking deals misery and destruction far and wide.

(c) The tendency to production on a large scale is mainly

due to the fact that the whole world is now one big circle of producer-consumers, every part of the world exchanging products with every other part, and to the enormously greater facilities of transport. Industries are largely localised to countries and districts where either the raw materials of the industry, or the necessary mechanical power, or some other condition favourable to the particular industry, is most readily obtainable, and the goods are then moved over vast distances. With the localisation of industries and the radiation of goods from the big centres to all parts of the world; with the remarkable development of the art of banking, relieving industry of the necessity of using large masses of coin or bullion: a vast change of another kind has gradually established itself side by side with the concentration of production into large units—a change which in no small measure dominates all the rest. All the great industries of the world are practically wholly set in motion, and are to no small extent constantly under the control of what is known as "finance," the operations and management of which are held in relatively very few hands indeed. This finance is for all practical purposes nothing more than the manipulation of the vast credit system—not by any means what the man in the street conceives it to be—as consisting of a few millionaires and bankers who keep great hoards of gold and lend it out to finance industries.

We have already dealt fairly exhaustively with the subject of bankers' loans, and have also had some insight into the actualities of big loan issues offered for public subscription. Though expressed in terms of coinage, the loans consist almost wholly of transference of credits from the subscribers' bank balances to the banking credit of the nation, municipality, company, or firm contracting the loan;

which credits are drawn upon by cheque or draft in payment of goods, and cleared in the usual course of bank clearings. But though the members of the general public are the bank depositors and subscribers to loan issues, the manipulation of the loans are in the hands of bankers and a few wealthy financing houses, planted in the several capitals of a few countries in Western Europe and the United States. The business of financing has almost become a species of heirloom, requiring as it does a special kind of experience, exclusive knowledge, and traditional reputation, frequently remaining in the hands of a family for generations in succession. We shall have something further to say on the subject presently. For the moment we only want to deal with so much of the question as is necessary to make understandable the part which finance plays in the periodic movements of prosperity alternating with depression so markedly obvious and regular practically throughout the whole of the industrial world. The problem of currency, so very much to the front already—inevitably so—in the course of our investigation, will, I trust, be finally disposed of, as far as it lies within the borders of our scope and purpose, in the next two chapters. As yet we have had no opportunity of realising how extremely delicate and sensitive a piece of mechanism our present currency system is. The formula of "unstable equilibrium," applied by Mr. Herbert Spencer to the phenomena of life, would not be an inapt description of the state of the currency, unless it be that it is much too mild. It depends for its precarious stability upon a psychological state, which is itself the victim of many currents and cross-currents. For the moment we must take this unstable equilibrium for granted, and just see how it applies to the immediate subject under consideration.

We will start the consideration of the trade cycle from the point when it is just beginning to recover from a slump. In the course of the descent into the trough of depression, production had been brought to a very low ebb. Many firms had gone bankrupt, others had voluntarily given up business, some stopped work for the time being, while many more had kept their machinery going half-time. Those who had personal savings were chary of lending or investing; the bankers, to avoid a drain on the gold reserve—the inevitable concomitant of a severe trade depression—were charging high interest; all things, apparently, conspiring to deepen and widen the depression. But while production was being kept down to a minimum, the accumulated stocks were gradually being consumed, until at last the effective demand of those who had saved credits on production began to overtake the available supply, and prices began to rise. The rise of prices and brisker demand open up new vistas of profits. Factories which had been running half-speed take on some of their old "hands" and employ new ones. These newly employed workers, in bitter need of many things, now swell the effective demand, and prices rise still further. Effect inevitably follows cause. Some of those who had shut down or relinquished business, as also those on the look out for business openings, seeing chances of profits, launch out into production. With each extension and speeding up, with each new enterprise, more workers are brought into the field of effective demanders; and every increment of effective demand tends to sustain or enhance prices, while yet the supply newly inaugurated fails to overtake the keen desire for consumption of many things of which the newly employed have for so long been deprived.

Man is essentially a creature of moods, governed by

impressions. The investigation of causes falls to the lot of but very few; and the mental mirage which constitutes most people's view of the economic structure serves effectively to obscure any chance glimpse of the true causes. With improved markets, with demand and profits rising, confidence is inspired, and the pessimism of the slump quickly gives way to a buoyant spirit of optimism. Banks are more willing and able to lend their credit, those who have saved are now prepared to invest, and the manipulators of finance find a ready field for floating new ventures, or for raising additional capital for extending and enlarging established enterprises. Limited liability companies are formed in many places throughout the world, nations and municipalities borrow for initiating more or less remunerative undertakings, and merchants are eager to speculate in anticipation of future demand, thus setting production in motion. Finance has long since ceased to be local or even national, the stock of many loans—incomprehensible in their total magnitude—being a huge mass of floating credit held in many countries, and frequently changing hands. With the return of confidence and a ready supply of financial credit, production goes apace, and the old conditions of each producer by machinery turning out goods on a large scale gradually return. But with unemployment at a minimum and the consequent widening of effective demand, with some rise in wages and salaries and a general increase of income amongst the employing class, with bank credits ready to back up reliable industries at need, the gradual acceleration of production does not outstrip the effective demand for some years. Local and seasonal waves are never absent, and even in times of greatest relative prosperity there are always some who complain of bad trade—not a few of them from sheer habit, as merely expressing some feeling

of disappointment at not doing so much as they expected or should like to. But taken as whole, the wave of prosperity in course of the world's "industrial" history has hitherto extended to somewhere about ten years.

In course of time, however, production at last begins to outstrip effective demand. There would seem to be no inherent reason why it should, since the obvious remedy appears to be to so apportion the incomes that the effective demand shall always equal the supply—the greater the supply, the more there obviously is for being distributed in incomes. But this is a matter which will be dealt with more fully presently, and again when we come to consider possible remedies. For the moment we must take the facts as we find them ; and these are that, inasmuch as a great number of people are contributing surplus wealth to the stream of production the claims on which are owned by others, their effective demand is limited to just that quantity, and no more, as is represented by the currency they receive in wages, salaries, and so on ; and if those who do hold the claims on that surplus wealth are too few to consume the unduly increased supply at the old prices, prices will be depressed below the margin of profitable production. When manufacturers and dealers find themselves with unsaleable stocks on hand, the result is, of course, a restriction of production, when many of the wage-earners are discharged to swell the ranks of the unemployed. This, obviously, further contracts effective demand, making the glut still more pronounced. That, in turn, causes further restriction of production, more workers are thrown out of employment, and demand still further lessened. And so the snowball adds to its volume as it is being rolled along. Bankruptcies are on the increase, confidence becomes shattered, and creditors are eager to collect their accounts. Want of confidence in

the world of commerce always has the tendency, as we shall see later, of causing a drain on the metallic currency. Partly in self-protection, and partly, no doubt, because bankers are subject to an attack of "nerves," the same as the rest of us, particularly as their risk is so much greater, bankers are constrained to raise the rate of interest, and to otherwise restrict the issue of loans by insisting upon security convertible on the instant. Sometimes, as in the United States in 1907, the depression is accompanied—or perhaps, caused—by what is known as a monetary panic, when many thousands of people act more like maniacs than rational business people. But the restriction of financial assistance—in effect, the withdrawal of a large proportion of the necessary implements of industry—has, in turn, the effect of still further intensifying the depression. Many legitimate undertakings for which there is a real demand, and which could be carried through successfully, are hampered or stopped for want of financial accommodation which would be available in normal times. The banking business is a practical monopoly in a very large sense ; and while all monopolies due to concentration of large capitals and doing business on a large scale have their distinct economic advantages—the monopoly of banking probably more so than any other—the disadvantages and the widespread character of their ill-effects are proportionate to the scale of their magnitude. There is no doubt that the restriction of financial assistance in times of trade depression considerably aggravates the evil ; and it is at least arguable that the evil could be considerably minimised. And so between the two causes—the supply overtaking effective demand and the restriction of the credit-currency—the depression descends to its lowest ebb, and then the flow sets in once more, and the cycle begins over again. The phenomenon has been familiar for

a long time to students of economics and business men, and many a brain has been puzzled to discover the true causes and account for its periodic recurrence.

We are now in a position to get something like a comprehensive and clear grasp of how demand operates and controls production. Leaving out of account the purely domestic work—no inconsiderable portion of the total volume of production—only in the industry of agriculture—and even there to but a very minute extent—does the consideration of “usefulness” enter as a conscious motive in the planning of production. The small allotment-holder who produces solely or chiefly for his own consumption is moved by the consideration of his prospective needs; and even those who farm on a larger scale give some thought to the needs of their own households, and reserve, perhaps, some small part of their farms to the cultivation of products intended solely or mainly for home consumption. In all other industries the consideration of “usefulness” practically never enters as a motive at all. The vast majority of producers—workers for wages, salaries, or fees—have neither part nor interest in the purpose and destination of the results of their labour. “Theirs not to reason why,” but simply to do that for which others are willing to give them claims which will enable them to take what they want from the stream of production. Those who possess capital and are prepared to employ it, together with what they can get on loan, in some enterprise are guided in their choice solely by the “conditions of the market”—in other words, by engaging in producing (or placing their children in a position which will later enable them to produce) that for which they estimate there is likely to be a continued demand. In a general way, whether the enterprise upon which people

are engaged is useful, useless, or even pernicious (short of being illegal or held in general contempt), has practically no influence whatever on the course of trade, manufacture, or professional occupation. No doubt some professional men feel a legitimate pride in being engaged in honourable and useful occupations, and there is also some sort of rough popular classification as to the worthiness of employments and occupations—though as often as not that classification is of a peculiarly topsy-turvy character from the ethical or rational standpoint. But the pride is, after all, only a secondary consideration, and frequently no more than an after-thought. The professions, for example, of teacher, doctor, or dentist, may be considered as equally honourable and useful, yet there is no eagerness to bring up children to the teaching profession, though there is at present a distinct scarcity of competent teachers.

A striking passage in a leading article of a recent issue of the *Westminster Gazette* throws a fierce light on the subject :

“Mr. Snowden,” says the editor, “paints a lurid picture of the armament firms behind the scenes and the pull which they have on the Governments in virtue of their great interests and capitals. That is not negligible, but among these interests we must include labour, which, so far as we have observed, always wishes Woolwich and Devonport to be working at high pressure. The armament firms, however, exert their pressure even more by their control of science than by their command of capital. The highest brains are applied not only to inventing new types of armaments, but to superseding them as soon as they are invented. Always their cry is, ‘We have something better which you must have, something

which, if it passes to another Power, will be absolutely fatal to what we gave you yesterday.' So the competition in armaments becomes exactly like the competition in millinery, with its endless endeavour to prevent womankind from wearing the hats of yesterday. If we could only get the brains as well as the capital diverted to some more profitable channel, the prospect of nations would be sensibly improved."

While the economic waste involved in the useless competition in armaments appeals more readily to our imagination, yet, apart from the frightful consequences of war for which armaments not only stand as symbols, but are in no small measure the actual cause, the waste for which the competition in millinery may be taken as the symbol and expression is of far greater economic magnitude and consequence.

It is not within the province of economics, as has been pointed out, to condemn luxuries, however extravagant and freakish, nor yet even "useless frills." It is not the positive side of the effort given to the making of the frills that matters, but the negative side that the effort so expended might have been employed in the production of those necessities and comforts which is denied to so many; and in the fact that the producers of the useless frills must be provided with necessities and comforts out of the labour of others—in plain terms, that, in so far as their services minister to the manifestly freakish and useless, they are nothing less than parasites on the community of workers, who are made to provide them with sustenance and comforts, while they contribute nothing useful in return. What is, however, of equal or, perhaps, of greater consequence is the fact that, even in the production of admitted necessities, much of the services now given, as we shall see more clearly presently, are uselessly dupli-

cated, triplicated, and quadrupled. In other words, that very frequently the services are so badly organised and adjusted that many are employed in doing something which could be done just as efficiently, and with no greater effort, by a few; and thus much of the labour is really wasted—labour that might have been employed in creating additional wealth.

And yet we are faced with the curious paradox that, under prevailing conditions, it is frequently better that men should be put to employment at wages by those who hold claims on production, however useless the work upon which they are engaged—digging holes and filling them up again, if you like—rather than that they should remain wageless; by which is meant not better for those so employed, which is only too obvious, but better for the economic condition as a whole. Nay, we can go much further than this. Under prevailing conditions, it is not unfrequently the case that the actual destruction of wealth, while, of course, entailing loss on individuals and insurance companies, is of clear advantage to the collective economic position of the nation. This startling proposition we shall make good before we are done with the subject under consideration.

We are now prepared to take a general survey of the industrial position and mechanism as governed by existing conditions. So that our conception of the matter may stand out "clear cut at the edges," it will be of advantage to re-state briefly the sense in which we use the term "production," and the image we have in our minds of what we call the "stream of production." All services whatsoever, whether purely personal, or that which we call professional, or the services of all kinds performed in, and incidental to, the production and distribution of

tangible commodities, are classed as production. And the "stream of production" is conceived by us to contain all these services, though some of them are consumed in the act of being rendered. There is nothing in this image which does the least violence to the economic reality for which it stands ; and, on the other hand, it is of inestimable assistance to the mental grasp in enabling us to form a generalised idea of what might otherwise have split up into a multitude of inconsequential details, none of them material to the main economic issue. This premised, we can proceed.

Many millions of people the world over are engaged in filling myriads of conduits which are feeding the main stream, from which there is continuously emerging a heterogeneous multitude of utilities designed to satisfy all sorts and kinds of human desires. But the right to take utilities out of the stream is portioned out by means of credit tokens or checks, entitling each holder to so much as is represented by the checks in his possession, each check standing for a recognised unit of value. The portioning out of the credit checks is governed by what we know as the law of "Exclusive Access to Superior Fertility." In so far as productive efficiency makes the "exclusive access"—in other words, in so far as the particular skill, due to training or to ability or aptitude more or less rare, constitutes a condition of relative scarcity—the efficiency will command a higher income. But this higher reward of efficiency is only incidental, and not inherent. The higher income will come just as certainly, perhaps more certainly, to the owner of "exclusive access" which has nothing in the world to do with personal ability of any kind, as, for example, the Charter to Covent Garden Market, or the inherited ownership of land, mines, or capital. There is, indeed, under present conditions of

the minute subdivision of labour no possible means of measuring wealth-producing efficiency even approximately ; and nothing is more patent than the fact that the sharing-out of incomes has no relation to the amount contributed to production, measure it by what standard you will. We see in many cases men of ability making high incomes, and are apt to conclude that the amount of their incomes is the *exact* measure of their productive efficiency, as compared with the efficiency of those who earn smaller incomes. But this is so patently fallacious that it is scarcely worth pursuing the point. It is not by virtue of having contributed a thousand guineas' worth of wealth to the world's store that the gifted counsel gets a thousand guineas for defending some clever and rich scoundrel ; he gets it because his abilities are rare and happen to be in demand. Instead of adding to the world's store of wealth, he sometimes succeeds only in setting loose someone to prey on the store of wealth created by others.

Up to a point, "exclusive access" and productive efficiency may coincide. Thus, the modern "store" may advertise itself into fame by a combination of cleverly drafted advertisements coupled with the sheer weight of a huge expenditure. Now, the handling and distributing of goods in large masses from one centre and under one management very considerably minimises labour—which would be generally expressed as reducing costs. Since, then, the rendering of given services with less expenditure of labour is in the fullest sense equivalent to a higher rate of production, it follows that the organising ability—even though it consists in part in setting a large number of people to the apparently unproductive tasks of drafting, printing, and circulating advertisements merely in order that people may be induced to become buyers at the shop of A. B. rather than that of C. D.—is a distinct means to the

creation of additional wealth. Suppose that 100 people are set to the work, not of producing any actual utility, but merely to spread a huge net which will draw people into patronising a particular business house, if by so centralising the handling, distribution, clerical work, transport, and so forth, the labour of 150 people is economised, the result is a net gain of the labour force of 50 people. Taking prices as an obvious test, every reader will readily call to his mind one or more business concerns whose prices are distinctly lower than that of most shops selling similar goods, spite of their spending large sums in advertising. Of course, whether the nation as a whole gets the increase of wealth such as the fifty people set free are capable of producing depends upon whether those so set free are put to producing other wealth. If they are simply thrown on the scrap-heap, then the nation as a whole gains no increase of wealth ; though those who deal at the store in question gain at the expense of the displaced workers, who now drag out a precarious existence on the crumbs doled out by charity or the nation taxing itself, giving part of the utilities created by the rest of the citizens to the displaced workers in a form of poor law relief.

These millions who are in the act of filling the conduits which feed the stream are directed to their labours by what is, and by the anticipation of what is likely to be, demanded, without any regard whatever to utilitarian values. And the anticipation of demand on the part of those who set industry in motion are always based on data which have no approach to accuracy, which are often of a highly speculative character, and sometimes purely chimerical. Thousands of people are employed in thinking out and devising some trumpery thing for which they believe they can create a demand. Months and years will be given to devising some new games—diabolo or ping-

pong, for example—or to some means of distraction to fill up the time of the idle, surfeited, enervated, and vicious, frequently to fail entirely in their anticipations, and sometimes to create a temporary craze, as senseless as it is useless, only to sink rapidly into the limbo of the forgotten.

It would be a matter for fervent congratulation if our image of production as constituting a vast stream fed by millions of tributaries could be further extended to the conception of a mighty, beneficent Nile, branching away at its mouth into millions of rivulets, brooks, and rills, designed to fructify an otherwise arid soil, to spread its fertilising blessings far and wide to the uttermost corners of the earth. We could then picture in our minds that so soon as the aridity of the soil at any one spot makes a special demand upon its fertilising rill, tending to lower its level, the water of life from the stream, by its own gravitational force, automatically fills up the rill again, keeping up a uniform level, as is the nature of streams, throughout its length and breadth. Unfortunately, such a parallel breaks down on investigation, and our image would then cease to typify the true facts of the case. The gravitational force does not act automatically ; the soil at some spot may be arid to the point of breaking up into yawning fissures, yet no fertilising water will come from the stream to relieve its palpitating gasps. A section of the community may be in need of the very essentials of existence, while the gifts of Nature and the productive capacity of the community may be capable of producing all that is needed to make the lives of all its members worth living ; and yet that section may continue to be in dire need because the dyke gates are closed, and those who hold the keys will not use them.

The claims on production being distributed so very

unequally, some few holding so very much, while many others hold very little or nothing (the question of deserts is here neither at issue nor relevant to it), what gets into the stream is governed by a set of cross-currents exceedingly complicated in their operation, and it will require some clear thinking to get at a true appreciation of the facts. If that small portion of the community who hold the major part of the claims are bent on having Pekingese Chows as pets, silks of many hues with which to line their cots, scent sprays in silver bottles to sweeten the cots, servants in livery to attend to their wants, expensive furs to protect them from the winter cold, and manicurists to trim and polish their claws (I am quoting from the newspaper reports of the Pekingese dog show), there will be plenty of people ready to devote their time and energies to breed these pets and to provide the various things called for them by their owners, since in return for that they get some of the claims which enable them to draw from the stream that which they require to satisfy their own needs. The result, of course, is that the stream now contains more of Chows and the requisites for their pampering, and less of those other things which, presumably, those who now attend to the production of Chows and their wants used to produce before the Chows became the necessities of refined and aristocratic existence. Those other things may have been of an equally refined type, or they may have consisted of such common and vulgar things as clothes and boots—yes, even of such brutalising things as saveloys and bloaters for the consumption of the coarse crowd. Since neither clothes, boots, saveloys, nor bloaters, grow on roadside hedges, it is very certain that less of these will be in the stream if a number of workers who had been, or who might have been, employed in their production are employed instead in producing Chows and their requisites.

With the reduction in quantity of the common things the price inevitably rises—there is less of them to go round. Instead of the “useless frills” providing the “wherewithal to live,” it has just the very opposite effect of restricting the supply of common necessities, and of intensifying the suffering of the very poor.

Some years ago, by a curious coincidence, there appeared in a daily newspaper two passages exactly side by side in two parallel columns. One was an account of a “Church Parade” in Hyde Park; and the neighbouring column gave an account of a visit to the home of a poor match-box maker. Here are the passages as they appeared :

“Among many pets brought out for an airing was a small African cat, wrapped up warmly in its mistress’s moleskin furs. Dogs of all sizes and breeds make their weekly appearance, some pampered pets vying with their owners in the matter of fancy apparel.”

“Sometimes the children run about the house naked, waiting to be dressed, till the mother has finished a certain number of the match-boxes. Often they have nothing in the house to eat except the flour necessitated by ‘the business.’ Nobody complains. Nobody weeps.”

“Nobody complains! Nobody weeps!” What human tragedy is disclosed in those four words! And who dare say that the two are not the complement of each other!

We shall more readily get a grasp of the problem if we cut down in thought our economic unit to small proportions—say 1,000 people inhabiting an island isolated from the rest of the world. We have by now, I trust, quite assimilated the thought that income consists of utilities for consumption, and that the money terms are only a means for defining the measure of the income. We have not been able to escape the use of the expression “money” income in contrast to “real” income. In a strictly literal sense,

anything that comes in is an "in-come"; but in any other sense of economic value, money, instead of being an income, is, on the contrary, the tangible evidence of income having been given up to be consumed by others. The actual income accrues when the money goes out, not when it comes in—when it is exchanged for utilities. I am afraid it will take a great deal of hammering before the "man in the street" can be made to realise this. We are so accustomed to look upon parting with money as "spending" one's income, instead of getting it. With that conception is, no doubt, bound up the thought of saving—the desirability of postponing the enjoyment of a part of one's income to a possible time of greater need—in which sense "spending" means "enjoying," or getting it now, as contrasted with postponing the enjoying to a future date. Conceiving income in terms of money, many people have the notion that they have only to show that the income of a nation as a whole has increased in a given period, to make it evident that everyone must be better off, more or less. There is the income, they say; and even if the rich men get most of it in the first instance, they spend it, and then others get it. I have also heard the same contention reasoned in yet another way. After all, it is argued, the rich man has only one stomach to feed and one body to clothe; and though he may eat more and better food, and wear more and better clothes, the limit is soon reached, and, provided the additional wealth created is really considerable, he cannot consume it all, and part of it must, therefore, be left to be consumed by others. During the last decade the income of this country has increased by somewhere between 400 and 600 millions sterling per annum. Unless that money is hoarded—which is certainly not the case—some of that increase must get into the hands of the workers, and so there is

more income for everybody. Can mathematical demonstration go further?

Here is where our contemplation of an island people, working up from primitive beginnings, cut off from the rest of the world, will help us to a clear appreciation of the position. Following our usual method, we will express the income of that island in terms of ideal units, each unit representing, say, a quantity such as we are accustomed to get in exchange for a pound sterling. Let us say, then, that at some given time the total product of that island amounted to 100,000 units per annum, averaging an individual income of 100 units. Some years after, owing to the invention of tools or machinery, better organisation, more steady and strenuous application, or any other causes, the income has risen to 150,000 units, an average individual income of 150 units. Now, it is obviously clear that, if conceived in money terms, that increase is not necessarily averaged out amongst the islanders. Some few of the islanders may—in all probability would—have grown rich, by becoming possessed of much of the land, the capital, and the organisation of industry, and that the whole or the bulk of that money increase was added to their incomes. But how does it come out when conceived in terms of products and services? Now, in the early stages the wealth of the island consists of agricultural products, herds of cattle, the captures of the chase, growing timber, huts or log cottages, simple tools and utensils, dressed skins, coarsely plaited or woven fibre stuff for clothing, and similar simple things of utility. Now, if the increase to half as much again meant nothing more than a corresponding increase in the production of the same utilities, the few rich men would, perhaps, be physically precluded from appropriating that increase, unless they simply wasted or destroyed it. A few extra skins for wear or

ornament, a larger hut or log house, a little more of the simple food and clothes, is all that they could add to their schedule of consumption. But what actually takes place is that, with the invention of new tools and organisation, and the acquirement of claims on the services of many by a few rich men, new ideas and desires gradually spring up, and the character of the island products is largely changed. The rich men want mansions to live in, instead of huts or log cottages; and so a number of workers are set to producing the mansions. They want ornamental gardens and parks; and so a number of men are set to plant and lay out the grounds. They want ornaments and finery for their women-folk; and so a number of men are sent to collect pretty shells at the far-off coast, and to manufacture necklets, bracelets, rings, and other finery. They want wines and spirits to drink; and so a number of workers are set to plant and tend vineyards, to raise grain for the spirit vats, and to perform the requisite processes of manufacture. They want Chows and race-horses; and so others are set to breed, tend, and train the animals. They want lackeys to do them menial and ornamental services; and so many men are detached for this work. Some of them become addicted to vicious and abominable habits; and there will not be wanting those who are ready to minister to their vices, however degrading and unspeakable. And so the list may be extended indefinitely. (The reader is begged to overlook the mixture of the relatively simple with the quite modern in the list of wants; it serves to illustrate the point without doing violence to the argument.)

The result of such an economic change is that, though the total income of the island has increased from 100,000 to 150,000 units—though the producing capacity of the people has increased by 50 per cent.—yet the staple

products consumed by the bulk of the people may have increased but little, or not at all, or may even have decreased. At the start, 1,000 people were producing just those things requisite for subsistence and some sort of rude comfort. Since then a number of workers have been withdrawn from that production and set to producing luxuries for the consumption of the rich men. If, by way of illustration, we assume that, all told, the work of 400 people is now given up to the production of luxuries, though the producing capacity of the islanders has increased by half as much again, there will now be produced only 90,000 units of the articles of necessity, instead of 100,000 units, since there are now only 600 left for producing the necessities. But since these 90,000 units of necessities have still to maintain 1,000 people—the 400 engaged in the production of luxuries for the rich men, as well as the 600 workers engaged in the production of the necessities (we leave the few rich men out of count, as extraneous to the 1,000 workers, so as not to complicate the figures needlessly)—instead of the average income of the workers rising from 100 to 150 units, it has fallen to 90 units. It is idle to point to the fact that the luxury-producers are receiving money wages just the same as are those engaged in producing necessities. Juggle with money terms as you will, in the distribution of labour as premised, there will now be only 90,000 units of necessities available for consumption, instead of 100,000, as at first, or of 150,000, as shown by the statement of total income. Thus, the capacity to produce more wealth does not necessarily mean an increase of income to the workers. How the economic mechanism operates we shall see more clearly in a moment.

Again, with a view of giving clear-cut edges to our conceptions, we must use some definite numbers. Let us,

then, suppose that ten of the islanders now own the whole of the land and capital of the country, for the use of which they receive rent, interest, and dividend. The captains of industry (whom we shall throughout consider as part of the 1,000 workers, or producers) produce for a "market"—that is, they try to find out what is "demanded," and adjust their production accordingly. The question, then, is, What, in the given conditions, will be demanded? In other words, What are the economic forces which will decide the numbers that will be engaged in producing necessities and those engaged in producing luxuries? Can, for instance, the demand for luxuries by the ten rich men collectively be so great as to absorb the labour of half the wage-earners? And if there is some limit, what is it that fixes and enforces the limit? Now, in the first place, assuming a static condition both of the natural resources and productive capacity, we may lay it down as axiomatic that no more people can be employed in producing luxuries than can be maintained in working efficiency by the labours of the other workers who are employed in producing necessities. But since the producers of the necessities must themselves be maintained in working efficiency—else they would not be there to produce—the results of their labour must be assumed to be sufficient to create the necessities for the maintenance of all the islanders. If, then, for the purpose of this illustration, we assume that 90 units per annum (average) is the minimum requisite for the maintenance of a worker (and his family) in working efficiency, then no more than 400 out of the 1,000 islanders can be employed in producing luxuries, since, if more were so employed, the labour of those left to produce necessities, after allowing for their own maintenance if they are to go on producing, would not be sufficient for the maintenance of the luxury-

producers. But the assumption of a sustenance minimum is, of course, largely gratuitous, and is, indeed, the whole key to the economic position. Speaking broadly, the incomes of the rich—in true economic effect, their power to withdraw workers from the production of necessities and set them to producing luxuries—are just proportionate to the incomes that can be secured by the workers by any economic pressure that they are in a position to exert and make effective. The so-called minimum may be no more than a few handfuls of rice per day, as in India and elsewhere, or it may reach the sustenance standard of the English or American mechanic. The higher the standard of living of the workers, the more necessities will be produced, and the less of luxuries; the greater the incomes of the workers, the less in proportion will go to the rent of exclusive access in any form. In so far as higher wages tend to a higher rate of productivity, incomes will be increased all round.

The economic pressure, then, will operate in this wise: Wages being at a given standard, the "market" demand for necessities and comforts will reach a certain point. There will be a fairly constant demand, for example, for staple foods, houses, clothing, furniture, and many other things of an ordinary type. The employers, out for making profits—which, as we know, means no more than a share of the joint product—will go on producing these to the extent of the demand. Sometimes they will miscalculate, and produce more of some things than is in demand (at remunerative prices); and at other times the production will fall short of the demand. But the employers are not bent on producing necessities in preference to luxuries. They will just as readily produce wines, silks, jewellery, elaborate furniture, motor-cars, Chows, or any other articles of luxury, to the extent

of the demand for them. But the extent of the demand for these will depend upon the size of the incomes of the rich, just as the extent of the demand for necessities depends upon the size of the incomes of the wage-earners. Now, you have only to interpret income in terms of utilities to see at a glance that the more of the possible output of the wage-earners on the island goes in wages—*i.e.*, to the production of the utilities consumed by the wage-earners, which the organisers of industry will take care to produce to the extent of the demand—the less income in the form of luxuries and personal service there is left for the rich. Conversely, the more income in luxuries there is for the rich, the less income in necessities and comforts there must be for the wage-earners. Expressed in another way, the greater the number of those withdrawn from the production of necessities and set to producing luxuries, the less there are left to produce the necessities; and as the smaller quantity of product in the form of necessities has still to be shared out amongst the same number of consumers, it can only be done by reducing the share of the workers all round. As we have seen, though the producing capacity of the islanders has risen from an average of 100 to 150 units, yet the income of the wage-earners may fall to 90 units or less. Given, therefore, a static state of productive capacity and enterprise, when one says that the incomes of the rich have risen, it means in effect that more of luxuries is being produced in relation to necessities; and when one says that (real) wages have risen, it resolves itself in fact to a larger production of necessities in relation to the production of luxuries.

But most modern economic states, in normal times at any rate, are not stationary, but progressive; and it is a condition precedent to economic progress that part of the

total income shall be consumed neither in luxuries nor in necessities in the ordinary sense, but in the creation of capital in various forms. This will consist of factories, machinery and tools, railways, trams, and other means of transport, construction of roads and bridges, docks and harbours, electric and gas works, business premises and organisations to facilitate the distribution of goods, opening up and development of mines and quarries, and thousands of other implements of industry, all designed to make production more prolific and to facilitate access to natural resources. Thus, 400 of our island people may still be withdrawn from the production of ordinary consumable commodities, but only 100 or 200 so withdrawn will be put to producing luxuries, while the others will be engaged in producing capital. This will make no present difference whatever to the fact that the remaining 600 employed in the production of necessities must still be producing sufficient of these for the maintenance of the whole island community; and, pending the employment of the newly created capital in wealth production, the incomes of the workers can still average to no more than 90 units. But as the newly created capital is gradually getting utilised, the productive capacity of each worker will be increased correspondingly, and with that the total income of the community will grow in proportion. Whether out of that increase of wealth the wage-earners will get a corresponding increase of income is quite another matter. The increased productive capacity may be absorbed either wholly in the production of additional luxuries, or wholly in the creation of further capital, or in part of one and in part of the other. An increased capacity to produce wealth contains within itself no sort of guarantee of a proportionate increase amongst the various sections co-operating in the production. Apart

from modifications due to a sense of justice and equity, whether individual or corporate, whether or not embodied in legislative enactments, the apportionment of incomes will always be governed by the economic pressure which we know by the name of Exclusive Access to Superior Fertility.

So far we have assumed that all the workers on the island are in regular employment, each receiving some share of the total income. We must now carry our investigation a step farther. So long as a nation is chiefly agricultural, and no one is completely divorced from the soil, there may be very little accumulated wealth; but, on the other hand, unemployment and destitution are practically unknown. But with a large section of the community cut off entirely from access to the land, with the development of industries—particularly that of “machine” industries—depending upon large masses of capital, there arises the problem of unemployment, with its consequence of an entire absence of income. In speaking of the problem of unemployment, few of us appear to be conscious that we are “putting the cart before the horse.” We do not look pityingly upon the rich idler because he is unemployed, though some may think that he also is a problem that needs solving. Of course, employment, apart from moral considerations, is a means to an end, not an end in itself. We need the “things” which employment creates, not the employment. Since Nature will yield nothing for human sustenance without labour, then we must labour to live—unless one is privileged to live on the labour of others. The problem of unemployment will come up for further consideration in later chapters; but we must examine one of the main causes while yet we have in our mind’s eye the small island nation, which will help us to visualise the problem much more clearly.

In the first place, we must by no manner of means confound unemployment with a natural shortage in the abstract. I confess to having felt irritated, not to say disgusted, when, as I was fated to listen to some time ago, a well-fed and well-groomed individual—he was a cleric, too, by the way—contributed his share to a discussion on the social problem by the statement that it was a question of over-population: that the pressure on the means of subsistence was greater than Nature was capable of yielding. He was clearly convinced that there were some people “too many” in the world, and was as obviously brimming over with the smug self-complacency that he was not one of the “too many.” But when, *e.g.*, a number of people escape in a boat from a sinking ship, does the person in command explain that it is impossible for all to share alike, because then the pressure on the food contained in the boat would be too great? Is not that taken rather as a reason for cutting down the rations all round? Time enough to talk of too great a demand on Nature’s bounty when there is some approach to a more equitable apportionment of the products of industry amongst those co-operating in industry. There are, of course, local shortages; there are shortages from season to season of various raw materials of industry. These will entail local hardship, and will more or less disorganise this or that industry generally. A machine will stand idle when the materials which it is designed to manipulate have run short; and it will also stand idle when some part of the mechanism has gone wrong. It is one thing to say that the fluctuations in Nature’s supplies, both as to locality and in the sum total from season to season, will dislocate some industries, and should involve more frugal consumption for the time being; but quite another thing to make the general proposition that there are more people

than Nature can be made to support. If there were any approach to truth in the statement, it would be a reason for "cutting down rations," but not for a constant fringe of unemployment and destitution side by side with Chows in scented cots. There is far more unemployment caused by parts of the economic mechanism going wrong, and by the fact that the whole machine is defectively constructed and put together, than by a shortage of the materials of industry—as is clearly evinced by the regular trade cycles of prosperity alternating with depression, regardless of fluctuations in the supplies of the raw materials of industry. Indeed, the fluctuations themselves in the supply of materials are, as we have seen, largely the result of the impetus or laxity given to them by the prosperity or depression in trade. There we see both the mechanical and psychological factors having a much greater effect on the course of industry than the natural abundance or shortage of materials. Of course some unforeseen natural calamity is always possible; but more often than not men make their own calamities. There are clear indications that the nations "armed to the teeth," shouldering burdens which are fast passing the limits of endurance, must at no distant date precipitate a world catastrophe which will shake civilisation to the very foundations. The economic machine, primarily on its financial side, and through that in its industrial activity, will then suffer severe damage; and it may be that a differently constructed economic machine will, as a consequence, emerge from the ruins. But all that has nothing to do with Nature's bountiful response to human effort for subsistence. I have no sort of hesitation in stating most positively that—subject only to a change in mental conception which is necessary to the stability of any economic system—with a scientifically constructed economic machine, and the consequent

elimination of waste, production could be easily multiplied tenfold, and probably even with considerably less labour.

We must now return to our island community. So far we have arrived at the following conclusion :

- (a) Given an average producing capacity of 150 units per annum, and a subsistence minimum of 90 units;
- (b) Given a few rich men owning between them the whole of the land and capital, who demand luxuries, or capital, or some of each, to the extent of 60,000 units, which will absorb the labour of 400 out of the 1,000 workers;
- (c) Then all the 1,000 workers will of necessity be constantly employed, since the full labour of the 600 not employed in the production of luxuries and capital will be required to produce the necessities for the 400 engaged in the production of luxuries and capital, after having provided for their own minimum of subsistence.

Both the fixing of the 90 units as the minimum, and the assumption that the workers will command no more than the minimum, are, of course, purely arbitrary. In the conditions stated, the workers collectively would probably find themselves sufficiently bordering on the line of scarcity to be in a position to exact something more than the 90 minimum. In that case, the number absorbed in the production of luxuries and capital would have to be less than 400, since the producers of the goods consumed by the workers will have to be more than 600 if they are to get incomes averaging more than 90 units. On the other hand, if the average income that the workers are able to command is less than 90 units, then more than 400 can be withdrawn for the production of luxuries and

capital. The chief point is that, *So long as the rich men, who hold the claims on production, demand (and obtain) luxuries, or capital, or both, sufficient to absorb the labour of a number of men whose total income can only be provided by keeping all the rest of the workers employed in producing that income, after they have produced also their own incomes, then unemployment is positively out of the question, since the production of the luxuries and capital together with unemployment cannot, in the terms of the proposition, exist side by side.*

But what if the rich men cut down their consumption by half, and decide to hoard up the balance of claims on production which they receive by way of rent and dividend? All the better, I can fancy some of my readers saying; a number of the workers who were engaged in the production of luxuries for the consumption of the few can now be employed in producing additional comforts for the consumption of the many. But where is the demand for these additional comforts to come from? Let us see. Six hundred workers were producing 90,000 units of necessities, of which, however, they are entitled to draw no more than 54,000 units—their average wage of 90 units per worker—while the balance of 36,000 units formed the income of the 400 workers engaged in producing luxuries, secured to them by the claims owned by the rich men; and the 400 workers produced another 60,000 units, which constituted the incomes of the rich, in return for which they received the claims on the 36,000 units of the surplus wealth created by the other 600 workers. The rich men having cut down their consumption by half, they only require the product of 200 instead of 400 workers. If the 200 now released from the production of luxuries are put to produce additional comforts, *while wages remain the same*, there will be a total product of goods intended for the consumption of the

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workers of 120,000 units— 800×150 ; whereas the wages list will only total up to 90,000 units— $1,000 \times 90$. There will thus be a lack of effective demand for no less than 30,000 units of product, which the employers will find accumulating on their hands. This will bring down prices, with a consequent re-adjustment of the real incomes of both employer and employed. The money wages would buy more of what has been produced, while the employer, having in fact given up more in real wages, would get less as his share of the joint product. This would last until the gradual accumulation beyond effective demand brings down the price to a point which leaves little or no income for the employer. With that comes the slump, production is gradually reduced, with the consequent unemployment and destitution.

But this does not state the whole case. Not alone will the production fall by the 30,000 units which the rich have ceased to demand, but the fact of this absence of demand will recast the whole industrial equation. Let us be quite clear about this. We have accepted the proposition that, in so far as labour is in demand, it will be in a position to exact not less than a minimum of subsistence, which, for the purpose of our argument, we have fixed at 90 units. Whatever is produced by labour over and above the minimum which they can command will go to rent, interest, dividend, etc. But what do we mean by labour in demand? In demand by whom? In demand for what? In demand, of course, for producing the utilities called for by the owners of land and capital. The income of labour is, as it were, merely incidental to the production of the income claimed by the other two factors of production. As we have seen, if the income demanded by the rich men amounts to 60,000 units out of a total producing capacity of 150,000 units, then all must be

employed, since 400 workers must be employed to produce the 60,000 units of income for the rich ; while the labour of the remaining 600 workers must be employed to provide for the maintenance of the 400, after their own minimum subsistence income has been secured. While, then, it is true that labour is an indispensable factor in securing the income of the rich, it is indispensable to them just to the extent of the income they happen to demand, which may or may not coincide with the absorption of the whole, or any other particular portion, of the available labour force. To that extent labour must also get its minimum income, or there would be no income for the rich. What, then, will happen if the rich reduce their consumption to 30,000 units, while still receiving claims on 60,000 units, half of which they simply hoard up, and keeping wages at the minimum level ? Two hundred workers at a producing capacity of 150 units are required to produce their incomes ; and the number of workers which will be necessary to provide the income of these 200, after having secured their own subsistence, is just 300 —thus : Production of necessities, $300 \times 150 = 45,000$ units ; Wages : $500 \times 90 = 45,000$ units. The employers will, of course, endeavour to utilise the surplus labour for profit-making ; but so long as wages remain at 90 units, and the total consumption of those who are in position to exact as rent, dividend, etc., all but that which goes in wages and profit is no more than 30,000 units, then for every one over 500 that is kept employed there will be a surplus of 60 units, for which there will be no effective demand at the old price. In other words, what should have been the employer's share of the product remains unsold, and therefore inconvertible into the particular utilities demanded by the employer as his income. The tendency will, therefore, be to the employment of no more than 500—that is,

to an equilibrium between supply and effective demand. So we get the startling result that the reduction of consumption by one-fifth of the total possible product tends to reduce both the employment and the total product by one-half !

Note, then, the astonishingly paradoxical nature of the result. A nation is an aggregate of individual units, and that which is good for *each* individual should, *prima facie*, be good for the aggregate collectively. Manifestly, the less, *e.g.*, a farmer consumes of his farm-produce, the more there is saved for future consumption ; the less of the claims on production held by an individual are expended, the more claims there remain to be expended later ; the less there is taken out of the stream, the more there should remain in it available for future use. It should follow that if a community of 1,000 people is capable of producing 150,000 units, and then a few of its citizens who previously consumed between them 60,000 units now choose to be satisfied with a consumption of only 30,000 units, there is a producing capacity of 30,000 units available to be utilised either for sharing out amongst the rest of the citizens or for creating consumables or capital designed for future consumption. Six hundred workers employed in producing necessities had previously provided the income of all the 1,000 workers, and now there are 200 more workers available for producing necessities, increasing the possible output from 90,000 to 120,000 units ; and with no increase in the number of prospective consumers. All this would seem to be the most convincing reasons for an increased prosperity of the workers. Yet we have this extraordinary state of things : that whereas when the total demand on consumption was for 150,000 units, production kept pace with the demand, yet when the demand on consumption falls by 30,000 units, not only

is production reduced by that amount—to 120,000 units—but, in absence of modifying causes which will be dealt with in a moment, must inevitably fall to 75,000 units—just half the producing capacity. The fact that a few people are consuming less than they might, instead of leaving more to be consumed by the others, causes a shrinkage in production by one-half, throwing half of the workers into unemployment and destitution. (See p. 268 as to the significance to be attached to the term "Natural Law.")

Fortunately, the habit of hoarding has almost entirely disappeared in all civilised countries. Mainly with a view to earning interest, but also because of the safety and convenience provided by bankers, people keep their personal savings deposited in banks. The business of banking consists in transferring the claims on production deposited with them—in actual fact lent to them—by their clients on to others, who utilise them in withdrawing from the stream of production such products as are necessary to maintain a number of workers who are set to producing more wealth, either in the form of commodities, or capital, or both. The new wealth contributed to the stream creates fresh claims, out of which the borrowers from the banks undertake to return the amount borrowed, with interest. We have called these claims so used "fluid capital," in the sense that it is employed as an instrument with a view to producing more wealth, and is, therefore, conveniently classed with what we call "fixed capital," as a means to the end of creating fresh wealth, just as a house becomes "capital" when converted into a shop. There is obviously an important distinction in the two forms of capital, inasmuch as the "fixed" capital tends to increase human capacity for producing wealth, while the other only sets in motion what productive capacity there

is, instead of its remaining idle. Bearing this distinction in mind, the terms must serve—it is, unfortunately, not the first instance by many of a defective terminology in the science of economics which we must correct as best we may by clear thinking.

The rich men on our island, by depositing the claims on 30,000 units of product with their banker, which the latter lends out to employers, once more create an effective demand for the whole of the 60,000 units, and so once more restores the production of the island to its full productive capacity of 150,000 units; and in the event of a part of the borrowed claims being used for setting workers to produce capital, as is generally the case in progressive societies, the total product of the island will gradually be increasing. There will, in this case, be a certain re-adjustment in the distribution of incomes. Thus, the rich man, lending to the bankers at, say, $2\frac{1}{2}$ per cent., will get an additional 750 units, without diminishing the quantity of their personal savings; and a new middleman, the banker, would be introduced, who would, by lending at 5 per cent., also get an income of 750 units, for managing what is in effect a part or the whole of the currency of industry on the island. It will be a matter for future consideration whether the function of such a middleman could be performed more economically and effectively in some other way; but, in absence of some other arrangement, it is clear that the intermediation of the banker in the alternatives under review—*i.e.*, that of hoarding, on the one hand, and of lending out at interest and providing a workable currency, on the other hand—is a function of enormous importance, tending to do no less than duplicate the production of the island. If we count the banker as one of the 1,000 workers, his income can accrue by a redistribution, without either an increase in the total income or a reduc-

tion of the average income among the 1,000 workers. Thus, by cutting down the incomes of 749 workers by one unit each, you get the banker's income without altering the average. But the additional 750 units of income accruing to the rich men by way of interest can only come either by cutting down the average income of the workers to slightly less than 90 units, or by an increase in the productive capacity, as a result of the borrowed claims being employed in the production of capital.

For all that, breakdowns in the economic mechanism through what we stupidly call "over-production" take place periodically with unfailing regularity, and at all times there are more or less mild local and trade disturbances arising from the same cause. People have to go without things because a lot of things have been produced which remain unconsumed—and this is "over-production"! This state of topsy-turvydom is obviously not attributable to natural deficiencies, but must be the result of a crazy mechanism. Indeed, the result is topsy-turvy just because the mechanism is topsy-turvy. It begins, as it were, from the wrong end, and makes "the tail wag the head." Instead of first thinking out what is the national collective need and then producing to meet that need, production is an individual gamble, without any means of knowing what the other gamblers are doing, sometimes in anticipation of a demand already established, and at others in an endeavour to create a new demand, regardless of any real need or usefulness. On the one hand, there is a frantic effort to fill the stream, the income of the employing producers depending upon there being a demand for all their products at the anticipated prices; and, on the other hand, the demand is cut off by not allowing the workers sufficient claims on production to consume what has been produced. The result is that the mouth of the stream gets choked up;

and when the employers at last discover by painful experience that there is no outlet for their products, the sources of supply dry up also, to the loss of their own incomes, but with the most dire consequences to the workers whose output is no longer needed, because so much remains unconsumed. The disease is not "over-production," but "under-consumption"; and the cure for it is to so distribute the claims on production that there shall be no product remaining immovable, blocking up the mouth of the stream. The creation of surplus wealth is, of course, the very life-blood of economic progress, but surplus wealth, as explained in Chapter VIII., and as will be further dealt with in Chapter XVI., does not mean something left over and put aside for future consumption, but that which is in excess of what the producer of the wealth himself consumes, which is, nevertheless, in a constant and continuous state of being consumed in order to produce further wealth, most advantageously in the form of capital.

It is this disease of "under-consumption" that causes the congestion of the economic machine; and in absence of adequate therapeutic treatment (efficient co-ordination of function between the various parts), it is better to remove the obstruction by a surgical operation rather than leave it there to grow and fester. The clogging-up of the mouth of the stream arrests production at the sources of thousands of tributaries; and leaving out altogether the humanitarian aspect of the question, from the purely economic aspect of wealth production, more wealth is lost by stopping up the sources of supply than by even wantonly destroying sufficient of the congested accumulation to establish once more a free flow. Owing to our competitive system of production, by the aid of machinery, and with the striking contrast between the incomes of the rich

and poor, there is, perhaps, more often than not sufficient of this artificial congestion to make it economically advantageous that those who have a superfluous amount of claims on production should part with some of the claims to others who will use them, even if they give nothing that can be considered as useful in return, so that the congestion may be relieved. The British people, *e.g.*, are capable of producing vastly more wealth than they are producing now; and anything which helps to keep the economic machine in going order will generally yield a greater return than the wealth consumed unproductively, which helps to remove the artificial obstruction. But this is quite a different proposition from conceiving that the production of "useless frills" provides the "wherewithal to live." The labour which is given to the production of "useless frills" cannot also be given to the production, *e.g.*, of clothing and boots—the more there is given to the one the less there must be given to the other. The "useless frills," as typifying freak luxuries, constitute a part of the income of one section, while the clothing and boots, as typifying necessities, constitute the only income of another section. Apart from correcting breakdowns—an economic disease—the more useless frills the less clothing and boots, and *vice versa*. We shall complete our consideration of the problem in Chapters XVI. and XVII.

CHAPTER XIV

THE CURRENCY PROBLEM

We must now complete our investigation of the currency problem as far as it is judged to be essential to an understanding of the economic structure. The literature on currency in the English language alone would easily fill a good-sized library, and anything like a full treatment of this thorny subject is, of course, out of the question. Even the reader who has never seen the inside of a textbook on economics will probably miss some question made familiar to him by name—bimetallism, for example—which he would have liked to have had explained to him. I can only express the hope that I have succeeded in so evaluating the importance and relevance of the many issues involved as to have made a wise choice of just those points which are necessary to a clear grasp of the economic problem as a whole.

Let us recall for a brief space the sense in which we understand the term "production." In the vast and mysterious physical, chemical, and vital laboratory of which Nature alone holds the keys, the metamorphoses, transmutations, and growths take place which we can justly call production. The nearest that man has ever approached to producing anything whatever in that sense is in those very few of what are called "synthetic" sub-

stances—I am by no means vouching for the fact that complete success has ever been achieved in that direction—which are claimed to have been accomplished in some chemical preparations. For the rest, all that man can do is mixing, shaping, and carrying, however ingenious the machinery which he employs. For the study of certain aspects of the economic problem it is often convenient to sort out the many processes into extractive, manufacturing, distributing, and speculating; and for the study in detail of each particular process a much more minute classification is necessary. But for the purpose of understanding the broader issues of the economic structure as a whole, the term "production" as applied to human effort to make the products which Nature provides subservient to his needs and desires must be taken to include all useful services whatsoever, from preparing the soil and the extraction of Nature's materials to the putting of the finished commodity into the hands of the consumer.

We apply exactly the same consideration to the sense which it is useful for us to give to the term "currency." What is it that we are actually setting out to learn? Not the art of banking or financing in any or all of the many branches into which it had become split up and specialised. Neither are we engaged in a purely intellectual exercise as a means of developing the reasoning faculty—much as some of us may need it. We are out to get as firm a knowledge as we may of the general conditions of wealth production, so as to be able to form a tolerably correct view as to the efficiency of the wealth-producing structure and mechanism, judge of the nature of its faults and shortcomings, and contribute to the best of our ability to form a body of sound opinion and influence which will lead to such changes or reconstruction as will remedy those faults and shortcomings. To those of us who get but a small

share of the created wealth there is clearly a shortcoming somewhere. It may, of course, be that it is entirely within ourselves—that our wealth-producing efficiency is such as not to entitle us to a larger share than we get; but if so, we want to know wherein we fail, and to take steps as rapidly as may be to make ourselves more efficient, or at any rate to put our children in the way of becoming more efficient. If we get little because we have not learnt to get out of Nature as much as we might, then by all means let us learn how to get out more. But if the fault lies, at any rate in part, in a defective mechanism, then clearly it is all the more necessary that those of us who are least favoured by the present adjustment should be the most anxious to learn to understand it, and to endeavour to apply the appropriate remedies. The man who gets the big slice is little concerned to know why it comes to him; he is generally quite satisfied that he fully merits it; it is the man who gets the little slice who should want to know the why and wherefore. Unfortunately, the man in the street has a general conviction that there is not anything that he can know—anything really useful and informing that he can learn. Economics is to him some technical hair-splitting—an endless exercise in and wrangles about definitions—of the dryasdust order, which demands a vast amount of plodding and concentration, and in the end leads to nowhere so far as he is concerned. One is bound to say that, to a large extent, his conclusion is not far short of the truth.

Man scarcely advances a step or two in the art of producing wealth before he discovers that it is practically impossible for him to make any headway without the intervention of a debit and credit account. Before he has gone many steps farther in the specialisation of occupations, and in relying upon getting much of what he wants

from others in exchange for that which he makes himself, he finds that the simple contra account between himself—suppose him to be a mat- and basket-maker—and some of his would-be customers is next to impracticable. He can get on well enough with, say, one or more farmers; but when it comes to the tailor, the bootmaker, the cattle-breeder, and so on, somehow it cannot be managed satisfactorily. What is wanted is a form of debit and credit which can be "negotiated," and transferred from one to another, frequently through a long chain. He does not know this; he cannot think it out. All he does know is that somehow it does not work—that he could make a lot more mats and baskets—that there must be a lot of people who would like to have mats and baskets—but that he cannot manage the method of exchanging. The tailor says: "Oh, bother your baskets! Do you think I want twenty baskets? Go away with you!" And so he finds himself stranded. A chain of credits passed on by mere word of mouth from one to another through a long series would necessitate, first of all, absolute and universal integrity. But even the most perfect integrity is no guarantee against illness, climatic misfortune, or bad judgment. In the absence of universal integrity, what is wanted above all is some tangible evidence which will record the debt on the one side and operate as the instrument of credit on the other, coupled with legal means of enforcing payments. One of the earliest forms of such an instrument was the notched stick, each notch representing a claim for value given; and such a stick actually passed as currency. From the notched stick, and perhaps some few other simple substitutes for book-keeping, man gradually stumbled into employing a commodity currency, as has been explained in a preceding chapter. Its commodity value gave it a wide and ready acceptability as a claim which is

bound to be honoured; and with the establishment of an efficient medium of exchange an enormous impetus was given to the specialisation of production, resulting in the long-run in a vastly greater productive capacity and the accumulation of wealth. The function of a commodity is the giving of direct satisfaction to some human need; while the function of a tool is to facilitate the production of commodities, thus indirectly contributing to the same end. But just as a cutting tool will be more sure, reliable, and expeditious if given a sharp edge by grinding, so the tool which functions as the medium of exchange will be the more sure and expeditious the less it is liable to lose its sharp edge of acceptability from time to time. As the sharp edge is the necessary condition of the functioning of the cutting tool, so is the acceptability the necessary condition of the functioning of the exchange tool. Given that condition of acceptability, it matters nothing what substance the tool is made of. Practically the whole of this chapter will, by one road and another, aim at discovering what are the conditions requisite to securing the essential condition of acceptability. In a primitive state, the condition of being itself able to function in direct satisfaction of a desire—in other words, of being in demand as a commodity—would manifestly constitute the best, if not the only, chance of any substance gradually establishing itself as a firmly rooted currency. In course of time it was gradually discovered that the metals silver and gold possessed qualities which made them exceptionally suitable for the purpose of currency.

But as man advanced still farther in specialisation of occupations, in trading at longer distances away from home, and with many nations and tribes, he discovered that the very instrument which was so enormous a factor in increasing man's productive capacity was now actually

becoming a hindrance ; and that he could do much better by reverting to the practice of his early ancestors. So he went back to what is for practical purposes the same thing as the notched stick, except that the record of indebtedness is more explicitly specified. He went to paper promises to pay. Well no, not quite altogether. The paper promises kept on, and do keep on, becoming more and more as the years roll on, and of recent years they have become simply stupendous in their magnitude ; but there has always been some portion of the exchanges which were effected by the metallic money which had got established in use. True, the notched sticks did not specify payments in some particular commodity ; whereas the modern paper promises specify payments in one of the two metals, silver or gold, according as to which happens to be the standard of the country holding the credit. On one stick each notch may have recorded a debt for a measure of rye, on another for a measure of barley, and on a third for a measure of milk. Nevertheless, it may be taken as certain that, as a general rule, the debts were not paid back in rye, barley, and milk, but in mats, baskets, skins, or in any other commodity produced within the tribal circle. Just so, the paper promises, except to an amount so small relatively as to be negligible, are paid, not in gold or silver, but in goods produced within the world's industrial circle. And so the enormous volume of paper promises, together with a relatively tiny quantity of metallic money, act together as the medium or instrument whereby the exchanges of the world are effected. The object of our inquiry being to learn the conditions of wealth production, so as to discover if it is possible to increase the production, to make labour more efficient and hence less onerous, and to diffuse happiness more widely, what we want to know in connection with money is how far, and

in what way, the multiform medium acts and reacts upon the world's wealth production. Hence we want a name which will cover the whole of this structure of exchange which we are trying to investigate. There are important distinctions between the various instruments functioning as the exchange medium, which will be analysed in due course ; but we want some comprehensive term which will stand for the general conception of whatever functions as the medium of exchange. And so we shall call those instruments "currency," and when we want to specify gold and silver exclusively we had better call that "cash," or "coin." We know what it is we want to reason upon, and so long as we have a clear conception of the composite instrument by means of which the exchanges are effected we are on perfectly safe ground. The term "money" would answer well enough but for its distinct association in people's minds with metallic coin ; whereas currency is accepted to include any legal tender, even of paper. We have only, therefore, to give it a somewhat wider significance to include any instrument which, as a fact, functions in doing the same work as the legal tender. True, the paper, consisting of bills, drafts, cheques, promissory notes, and so on, breaks down at times, but so do the paper legal tender notes ; and, what is more to the point, so does gold in a very important sense indeed, as we shall see later, and as many of the owners of property let on old leases can testify. We want to know the causes of the breakdowns and consider the remedies ; but we shall not improve matters by burdening ourselves with an unnecessary classification. Where it becomes necessary to see the distinctions between the various forms making up the body of the currency, we shall do our best to embody them clearly in the terms of the argument.

The advantages of gold as a currency have been stated in words the initials of which make up the two words "D-i-s-h C-u-p," thus : Divisibility, Indestructibility (other than abrasion from wear), Stability (of value relatively to fluctuations in other commodities ; but as to that we shall have a great deal more to say presently), Homogeneity, Cognisability (by appearance, distinctive metallic ring, and easy chemical tests), Utility (better expressed as having commodity value), and Portability (owing its high value, which makes a small quantity command a great deal of other commodities in exchange). Five of these qualities are possessed equally by silver (the quality of Indestructibility in even a greater measure), but, relatively, the qualities of Stability (of value) and Portability are not so good. During the last fifty years there has been a great and continuous fall in the value of silver, and on that very account its quality of Portability also has further been lessened, since it would now require about thirty-nine times as much by weight to pay a sum in silver bullion as it would in gold. However, this matter has no particular bearing upon our lines of investigation, so that we need not pursue it farther.

What is of exceeding importance as a starting-point in our inquiry is, to disabuse the reader's mind once for all of the fallacious notion that he may have formed of the value of gold. It is quite a common thing to hear the man in the street say that the value of gold is fixed by law, to which fact he evidently attaches some very important meaning and consequence. It is really curious that so many people who have not the remotest knowledge of anything in economics should somehow have managed to have got hold of this fact. It evidently springs from their conception of the economic structure in terms of the Mercantile Theory, and they imagine that the fixing of

the price of gold by law somehow confirms, strengthens, and consolidates their grotesque monstrosity, and that it is one of the reasons why gold must command wealth. But all that the legislature has done is to instruct the Bank of England to give, weight for weight and quality for quality-less only by three halfpence in the ounce-coined gold for gold in bullion. The point really is that the Government makes no charge for seigniorage, everyone being entitled to take standard gold to the Mint and demand that it be coined into money free of charge. Why, then, should not one ounce of gold change for another ounce? Would there be any sense in saying that one bean is worth another bean of the same size and quality? Can it ever be worth less or more? Would such a statement convey any meaning? You cannot express the value of a thing in terms of itself—value is a ratio between two or more things. In certain extreme circumstances, and for a very brief period, it is possible for coined gold to rise slightly above bullion ; and in another set of extreme circumstances it is equally possible for bullion to rise slightly above coined gold. For all practical purposes, so long as there is no charge for seigniorage, the two are interchangeable, except for a very small commission as a remuneration for handling on the one side and saving delay on the other side. To save inconvenience at the Mint, by unequally distributed demand for coining, the Government makes the Bank accept the duty of giving coined for uncoined gold. The actual equivalent is £3 17s. 10½d. per ounce—that is, it would require just a few grains over the ounce to make four sovereigns—and the law makes the Bank pay the minimum of £3 17s. 9d. There is, indeed, a fluctuation, but it may oscillate to the extent of the odd three halfpence in the ounce—though in practice to rarely more

than one halfpenny. We can attach no meaning of value, or even price, to such a fact. We can learn nothing from it, and may dismiss it at once as an utterly useless piece of knowledge, apart from telling us that there is no charge for seigniorage.

The value of gold, then, can only be stated in terms of other commodities, and, except that it fluctuates less violently, it nevertheless fluctuates in value, as do all other commodities. In taking up the investigation from this point on, we shall find ourselves very quickly plunged into a sea of complexities, where we shall have to steer our way with the utmost caution if we are to escape mental shipwreck. I think it was Professor Stanley Jevons who said that writers on currency are often taken with a species of intellectual vertigo. Certainly, some of the curious notions that many people have about currency seem not far short of imbecility.

Perhaps the most important function of a currency is that of adjusting what is called the "coincidence" of barter. By means of it the tailor, whose coat is worth so many loaves, pounds of butter, pints of milk, and so on, can manage to effect all the exchanges, in spite of the great disparity between the value of his commodity and that of any of the others taken singly. With that we have already dealt sufficiently. The next important function is that of acting as the unit, or common denominator, by which values are compared and expressed. With that we have also dealt in a preceding chapter, but shall have to elaborate considerably further.

The first thing we have clearly to understand is that a rise or fall in price is not necessarily the same thing as a rise or fall in value. Both value and price can only be understood in the economic sense as a ratio of exchange between two or more things—price expressing

the ratio between money and the thing named. Now, suppose we ignore for a moment the money terms, and express a change of ratio between two things in terms of quantity only. Let us say that, whereas jam of a certain make used to exchange for butter at the rate of 2 to 1, it will now exchange only at the rate of 3 to 2. A little thought will show that this may be due to one of two causes: the value of jam may have risen owing to scarcity, or the value of butter may have fallen owing to abundance. The money price gives us, however, an indication of the true cause. Thus, whether the price of jam had changed from 6d. to 8d., or the price of butter had changed from 1s. to 9d., the ratio of exchange between the two would in either case have been altered from 2 to 1 to 3 to 2. But in the case of the change being in the price of jam (while prices generally remain as before), it is clearly a rise in value of jam, owing probably to scarcity of fruit, or sugar, or both; whereas the change in the price of butter is clearly a fall in the value of butter, owing probably to a plentiful supply of cattle feeding stuffs and favourable weather generally. But supposing we have before us a rise or fall in the price of one article only, without any indication as to whether there has been a rise or fall in prices generally. What we have before us then is a change in the ratio of exchange between money and some one article named; and just as, in the case of a change of ratio measured in quantity only between jam and butter, without other indications to guide us, it may be either a rise of value in the one or a fall of value in the other, so in the case of change of price it may also be either a rise in the value of one or a fall in value of the other. Thus, if wheat has risen by so many shillings in the quarter (when not due to a tariff), it may be either a rise in the value of wheat or a

fall in the value of gold; if wheat has fallen in price, it may be either a fall in the value of wheat or a rise in the value of gold. A given sum of gold will buy more of things when it is scarce, but less of things when it is abundant. We have, however, a fairly substantial guide from prices generally. If prices generally remain as before, and only one or a few things have risen or fallen in price, it is fairly clear that there has been a rise or fall of value in that one or few things. But when there has been a general rise or fall in prices—and particularly when there is a continuous progression one way for some time, without any indication of an exceptional increase, or an exceptional diminution, in wealth-producing capacity—it may be taken as certain that there has been a rise or fall in the value of gold. Always bear in mind that the rise or fall in the value of gold is the inverse of a rise or fall in prices—*i.e.*, when gold rises prices fall, and when gold falls prices rise. Professor Stanley Jevons estimated that in the twenty years between 1789 and 1809 gold fell by 46 per cent.; then in the subsequent forty years from 1809 to 1849 the value rose by no less than 145 per cent.; and then it fell back between 1849 and 1874 by at least 20 per cent. There was then a considerable period of falling prices, but due largely to the rapid development of industry and the opening up of new sources of wealth in America; but during the last twenty years or so (to 1913) there has been again a continuous rise in prices of about 20 per cent., due almost certainly wholly to a fall in the value of gold.

But while the periodic and, relatively, slow-moving fluctuations in the value of gold enter, of course, as important factors in the progress of industry and the distribution of incomes, it is rather the frequent—indeed, practically constant—small fluctuations this way and that

in the value of the currency as a whole, gold, silver, and paper taken together—of which, as we know, metallic money forms such a small proportion—that constitute the most important factor in the course of industrial development, and one of the issues before us that is extremely difficult to apprehend clearly and to follow in all its intricate details and consequences. We shall do well to start the consideration of it from the beginning, and pursue it step by step.

As far as may be, we shall adopt our usual plan of developing the subject progressively; but owing to its complexity the reader must make some liberal allowances. The difficulties chiefly arise and become accentuated (1) as the currency changes from the strictly monoform, be that cowrie shells, bronze, copper, silver, or gold, into a multiform currency of two or more metals; (2) as paper promises to pay become part of the currency, displacing "commodity" money; (3) but chiefly when, in addition to serving as a medium within the limits of the national boundaries, it has also to meet the requirements of trading with other nations. It is generally difficult, however, to disentangle the complications arising from the currency having to function in international exchanges from those which are, as it were, inherent to the currency structure, even if it had to function for home exchanges alone—the two so frequently merge into, and overlap, each other. It is not, therefore, possible to split up the analysis into two distinct sections; but as far as possible we shall follow up the consequences of the home functioning before we plunge into the much more difficult international aspect.

Let us, then, revert to our more or less primitive nation, which has at last succeeded in establishing in its midst a

currency of general acceptability, which we will suppose to consist of gold. At the starting-point, gold must have already established for itself a fairly stable exchange value in relation to the other commodities produced within the national circle, else it could not, in the conditions which we have under review, have come into use as a currency. The exchange value was, of course, the consequence of the relation between supply and demand; and equally of course, it must have been subject to fluctuations in the event of any change in the relation between supply and demand.

When, in addition to its use for ornaments, gold became in requisition for use as an exchange medium, a fresh demand was created which would obviously have its effect on the exchange value, unless a fresh supply of corresponding dimensions were created at the same time. We have seen that the introduction of a currency is a tremendous factor in the increase of production, by facilitating exchanges—indeed, by making exchanges in many cases easy and sure where before, under barter, they were next to impossible. With each step in the increase of production, and the consequent increase in the number of exchanges, there is a further increase in the demand for gold as the tool of exchange. With each increase in demand, in absence of a corresponding increase in supply, gold will inevitably rise in value. In the exceptional degree of the quality of Divisibility which they possess—*i.e.*, of being either divided up into smaller masses or of being re-fused into larger ones, without appreciable loss—gold and silver have particular advantages in meeting large differences in value; though each falls short of ideal perfection at opposite ends. To say nothing of *exceptionally* high value, even at its present value gold could scarcely be divided up into handling

capacity for small purchases, while silver would be too bulky for large purchases. It is for this reason that nations have adopted a mixed currency of several metals, more recently in the form of a subsidiary "token" money—*i.e.*, containing less than the metallic equivalent in value of the metal that happens to be the standard coin of the nation—and is therefore made legal tender for specified limited sums only; in this country, silver for £2, and coppers for 1s.

It is worth while digressing here for a few moments to correct from a fresh standpoint, only just opened up by the stage we have reached in our study, the inherited and almost ineradicable notion that gold has somehow a kind of "innate" value—something, as it were, "born" with it and inseparable from it—unaffected by outside conditions; "concentrated wealth" some writers call it. Its past and present value depends, as we see, largely upon the accidental fact that it has been so widely adopted as currency, giving it an enormous demand for use as a tool, in addition to whatever demand it has for the direct satisfaction of human desire. Gold possesses certain qualities which make it fit to perform the function of a "commodity" currency better than any other substance that we know at present. Nevertheless, as we hope to see clearly before we have concluded this subject, the need of a "commodity" currency at all—under present conditions forming merely the slender basis for supporting the gigantic structure of a paper currency—is of a distinctly psychological nature; in other words, is made necessary by a certain mental attitude which is not necessarily, or even probably, permanent. There is a world of difference between a "commodity" tool of exchange and most tools employed in industry. One cannot even in imagination conjure up a condition when we could dispense with the

"cutting-edge" tool in its many forms—the plane or planing machine, for example—but it is the easiest thing in the world to imagine conditions in which a commodity currency can be entirely dispensed with, since even now we have gradually brought down its use to a tiny fraction of the total. At any rate, the present value of gold is the result of its being in demand for two separate purposes; but what its value would be if it were suddenly and wholly demonetised it is hard to say, except that there would certainly be a terrific slump. How, for instance, would the stability of value have appealed to one who had hoarded up a quantity of gold in 1789, on finding in 1809 that its so-called purchasing power was cut down to about one-half? We shall have something further to say on the value of gold in so far as it is employed as currency when our subject is more fully developed.

We now come to the important task of finding how a change in the relation of supply to demand of gold gets translated into a rise or fall of general prices. We always speak and think of buying and selling goods, never of buying and selling money; hence, as a matter of course, whenever there is a rise or fall in prices, we naturally interpret it as a rise or fall in the value of goods, never as a rise or fall in the value of gold. But actually the one who sells goods buys money with the goods, just as the one who pays the money really sells it for the goods. True, the seller of the goods only takes the gold with the object of giving it for something else that he really wants to satisfy a need or desire; but we say of the latter that he buys a hat from the manufacturer, although he does not mean to wear the hat, but only buys it to sell again. When we come presently to consider the currency as a whole, we shall be able to realise more clearly that what

the seller really buys is a "claim" or a "right"—a right to demand an equivalent of that given up to be consumed by others. When one comes to reason the matter out at all, it is readily seen that a "right" is what one practically always buys, at any rate as a member of civilised society, where laws are made and enforced. You buy an estate, and you then say, "It is mine." But in what sense is it yours? In absence of law and social consent (the basis of law), it would be yours only so long as you could defend it against all comers; and when ownership depends upon who is the strongest, there is clearly no point at all in buying, since, whether you buy it or take it from someone who is weaker, you can only keep it by defending it against all and sundry. What you buy is the legal title, with the implied social protection against violence and deprivation. Just so, when you buy currency for goods, you buy the right to demand other things which will complete the barter of something that you want for that which you gave up. But where gold is the unit of value (a matter which will be dealt with further in the next chapter), the contract is necessarily for so much gold.

It is always difficult for the mind to focus to a point, as it were, a great multitude of small causes which finally bring about a cumulative effect of magnitude—a vast interlacing of minute capillaries which contribute to a vital blood circulation. Most of us are conscious to some extent that when we have more money than usual we spend it more freely; we buy one or more things at a price which ordinarily we should have done without on account of being too dear. When new gold-mines are discovered, or means are found for making existing mines yield better results for labour expended, the increase in the supply leads the owners to spend the gold more freely. Presently the prosperity of the mine-owners spreads to a greater or

less extent to their wage-earners. The latter then also spend their increased wages more freely, though of course on a proportionately smaller scale. The manufacturers, merchants, and tradesmen, finding that they can borrow on easier terms, and that the goods will sell at higher prices, are ready to pay more for their raw materials and launch out in larger trading. In effect, the gold is being sold cheaper, having fallen in value owing to a greater supply in relation to goods the supply of which has not increased relatively.

As a general rule the wage and salary earners—those with fixed money incomes—find themselves considerably mulcted in this process. Money wages do not increase as a matter of course with a rise in prices. There is, as we have seen, a constant tendency to fluctuations in prices, owing to periodic changes in the supply of commodities, due to causes which have been analysed. In absence of a “sliding-scale” arrangement operating readily—a matter that would be very difficult to adjust—wages cannot very well rise and fall daily, weekly, or monthly, with every fluctuation of an upward or downward movement in prices. When, therefore, the rise in prices becomes due to a cause which proves to be of longer duration and of cumulative effect—*i.e.*, an increased supply of gold—the wage or salary earner is the last to make good his claim to an increase, though he may soon become conscious that his money does not go as far as it did. When he does get some increase, it rarely keeps pace with the depreciation in the value of gold, due to some permanent cause of increasing supply. During the last twenty years or so, while the value of gold has fallen by about 20 per cent., it is estimated that money wages have risen by no more than about 12 per cent., leaving the wage-earner about 8 to 9 per cent. worse off in real wages.

Fortunately, there are causes which counteract to a very considerable extent the depreciation of gold that one would conclude must arise from the known increase in the output. Uninfluenced by other factors which enter into the equation, some of which have already been explained (see p. 160), the fall in value during the last twenty years must have been much greater than it has. On the other hand, while the continuous fall in the value of gold is largely arrested by other causes than mere quantity, the entrance into circulation of a vast quantity of paper currency introduces a cause of constant fluctuation in the currency medium taken as a whole. We must now follow this up with considerable care.

In the first place, it is necessary to recall what we have learnt in preceding chapters—that the mere quantitative relation of supply between two things does not alone decide that the thing of which the supply has increased must of necessity fall in exchange value in relation to the thing in which the supply has remained stationary or has decreased. There is the element of demand to be taken into account, which may have increased at the same time either from some material cause, such as a new use having been found for the thing, or from some purely psychological cause, as a change in taste, fashion, and so forth. Gold is in demand for two quite distinct purposes—in the arts and as a medium of exchange. Now, in its use as a medium of exchange there can be an increase or decrease in demand arising also from two separate causes. We may repeat here with advantage an illustration we have already had before: Smith of London owes Brown of Manchester £20, while Brown owes Smith £25. There are three ways in which these two accounts can be settled: the two sums in gold can cross each other by registered parcel, requiring the use of forty-five sovereigns; or Smith

can wait until he gets the £25 from Brown, and out of that send him back £20, requiring a total use of twenty-five sovereigns; or the two can credit each other on their books for £20 *per contra*, and all the gold required will be a balance of £5 from Brown to Smith. Thus the use of gold can be economised by a simple contrivance. There is, however, another very important cause of variation in the use of currency in any form, and that is simply the quantity of transactions that have to be carried through. The greater the production and trading of a nation becomes both at home and abroad, the more currency it will obviously require to carry through the increasing number of transactions. Hence, whether there is more gold than is required for use as currency, or just enough, or less than is required (at the old prices), depends upon the state of production and trade, coupled with the economical management of its use.

We must now elucidate what is known as the Ricardian Law of the Distribution of the Precious Metals; but before doing this I cannot resist the temptation of briefly correcting what appears to be a quite common misconception as to what is meant by the enunciation of what we call a Natural Law, in all branches of scientific research. A true conception of what is meant to be conveyed by the statement of a Natural Law is almost of greater importance in economics than in any other branch of study, as we shall realise more fully as we go along, and is, perhaps, more particularly so in regard to the law which we are about to consider.

Perhaps the reader will catch the point more quickly and clearly by the use of an example. Some years ago a writer in the *Contemporary Review*—it was in relation to the question of free-will, but we are not obliged to step on to that quicksand—argued thus: “If we let a stone fall

freely from a height, we can predict the exact spot where, in conformity with the law of gravitation, it will reach the ground. But let loose a bird from the hand, it may alight on the ground, on any tree, on any part of the housetop”; the conclusion apparently being that, while the reign of law holds good in the inorganic world, it breaks down utterly in the case of sentient life. Well, now, it is simply not true that we can in an unqualified way predict accurately where the stone will reach the ground. We can only say what will happen *under strictly defined conditions*, else a strong gust of wind will falsify our prediction; and the extent to which a given wind pressure and velocity will deflect the object will depend upon the weight of the object. But, then, to the extent that we are in a position to strictly define the conditions, we can equally predict about the bird. I could safely venture to predict that a sparrow let loose from the hand in Hyde Park will not first alight in Phoenix Park, Dublin; indeed, I think I could safely predict that it will not first alight on Clapham Common. There are many things we cannot predict about the bird, because we do not know the conditions. But in this respect we are in no better position in regard to the inorganic world. If we do not know the direction of the wind currents, we cannot tell where an ordinary balloon will travel, but we are not on that account precluded from predicting that it will travel with the wind currents. Put shortly, there seems to be an inclination to conceive that what we call a Natural Law must be capable of being stated without qualification, as not being subject to modifications with changed conditions which may enter into the equation; but if so, we simply have no knowledge at all of such a law. What we say is that, reasoning by induction, we are entitled to say that, given certain strictly defined antecedents, there will be a certain consequent,

but that with changing conditions the result will vary as the modifying factor or factors. Since economics has to do with psychological factors in which the equations are frequently recast by varying conditions, there are always exceptions, which, however, do not invalidate our conclusions as to the general application of the law under normal conditions. The critical reader will, I believe, find this view of the matter of considerable help, particularly when he extends his reading on the subject, and comes across much controversy.

To come, then, to the famous Ricardian Law. No nation will keep for any length of time more gold or silver (whichever happens to be the standard) than is just required, in the given industrial development and economical management of the currency, to carry through the necessary exchanges; nor will it for any length of time have less than that requisite quantity. If the total of the metal in existence is small relatively to the total of exchanges amongst all the industrial nations, then less gold will buy more goods, and the relative need for purposes of currency will be less in proportion; and if the total becomes larger, more gold will have to be given for goods, and the quantity required will be proportionately increased. But the inevitable tendency is to a distribution of the precious metals amongst the various nations, each getting them in proportion to its trading requirements. Thus, supposing we imagine the world to have been consolidated into four industrial nations, A, B, C, and D, doing respectively volumes of exchanges which can be expressed by the figures 40 : 30 : 20 : 10, then, whatever the quantity of gold that happens to be in existence appropriated to the use of currency would get so distributed amongst them that A gets 40 per cent., B 30 per cent., C 20 per cent., and

D 10 per cent. What the reader should note particularly is that the quantity of gold required by each depends upon how the use of the currency is economised. In a country where the use of paper currency has become highly developed, and can be used safely and without hitch, less metallic currency will be required in proportion to the quantity of exchanges; so that a country like England, doing a vast trade, will require a smaller proportion of gold to the total of trading than do other countries, because its system of bank cheques and other currency paper has been so highly developed. But, as we shall see later, it is just the question of the point of safety in dispensing with gold and making paper do the work of exchanging that constitutes the most intricate and uncertain of issues of the currency problem. So far a certain proportion of gold has proved indispensable; and whatever that proportion, the tendency is for each country to get according to its needs.

But in what way does this tendency work out? The answer to this question takes us straight away into the currency issues as affected by its having to function in international exchanges. The distribution of the gold is brought about by what has been explained a little way back as to gold falling in value when it is redundant, and rising in value when it is scarce. In the country where there is more gold than is necessary to carry through the required exchanges, the excess of gold raises prices; while in the country where gold is scarce, prices fall—that is, less gold will buy more goods. What is the result? As the countries are trading with each other, merchants in the country where the goods are dear make a rush to buy in the country where the goods are cheaper, so as to make a profit by selling in their own country at the dearer price. What happens as a result is that the country in which the

goods are dear buys more from the country where the goods are cheap than the latter does from the former. As a general rule, as we shall have to deal with in greater detail presently, countries settle their reckonings with each other in *per contra* accounts, by means of bills of exchange and other paper documents. But in the case under review the excess of buying by the country in which the goods are dear leaves a balance to be paid to the country in which the goods are cheap, for which no bills are available, and that balance has to be settled in gold. Hence, as a direct outcome of the excess of gold, a condition is created whereby the gold flows from the country where there is the excess to the country in which there is a deficiency, until the prices are on a level. In effect, the country which is short of gold buys the gold, paying for it with goods. The buying of one country from the other then swings back to those goods only in the production of which the respective countries have some special advantages, when the normal buying and selling tend to balance each other, since in the long-run no country can buy from other countries more than she can pay for by giving her own products in exchange. In the case just considered, the excess of gold represents so much product given in exchange for the gold to the gold-mining country, and then the gold sent out to pay for the excess of foreign product, so that it is after all an exchange of products. In the end, a nation can only pay for the goods which she imports by the goods which she exports.

The number of exchanges necessarily increases both with each division and subdivision of production into separate processes, and with the general increase in the production of wealth; and the need for currency is increased in proportion. A quite considerable proportion

of this is economised in home trading by means of purely book-debts, which combine a number of exchanges into one settlement; and may even then be occasionally—though not very frequently—settled by contra accounts, so that no currency document changes hands at all. In the case of foreign trading, however, the system of book debts is relatively very small: in the first place, because some negotiable instrument for squaring accounts is always in requisition, so as to obviate the expense of sending metallic money in payment; and, in the second place, the transactions being mostly on a larger scale, manufacturers and merchants require the credits which they have for goods supplied for using in payment of wages, and for settling debts for goods bought; and the bills of exchange enable this to be accomplished by the intermediation of the banking system. Just as no specialisation of trades at all worth speaking of could have taken place without the introduction of a currency in some form, so the development of industry on modern lines could not have taken place—indeed, could not have approached to within measurable distance of it—without the introduction of paper currency.

The usual form of a bill of exchange is as follows:

£100.

Date.

Accepted, payable at
So and So Bank, at
such address.
JAMES BROWN.

JOHN SMITH.

One month (or longer, as the case may be) after date
pay against this Bill of Exchange to my Order the sum
of One Hundred Pounds for value received.

MR. JAMES BROWN,
Blank Street, London, E.C.

John Smith is then known as the "drawer" of the bill, and James Brown is the "acceptor." The forms of bills vary in certain minor respects, but these are the main features.

We must now give a very brief sketch of the operation of paper instruments in international trading, involving the exceedingly complicated subject of what is known as "Foreign Exchanges," in so far as that knowledge may help us to a clear grasp of the currency problem as a whole, towards which we are aiming.

In Chapter X., p. 139 *et seq.*, the method of settling foreign accounts by means of bills of exchange has been made fairly clear. There are at all times a great mass of such bills in the hands of foreign bill brokers and bankers, who are said to "buy" the bills, and who dispose of them to those who have to pay accounts abroad. We must first say a few words of what is meant by an "exchange at par." Strictly speaking, this term is only applicable as between countries whose monetary standards consist of the same metal—gold or silver. If the two countries have both a gold standard—which most Western countries have to-day—the exchange ratio of their paper currencies, if not influenced by any other considerations, when it is said to be "at par," will depend wholly upon the metallic value of their respective gold coinage. For instance, the gold contained in the 20-franc piece expressed in English money is 15s. 10*½*d.—that is its metallic equivalent compared to the sovereign. Hence the exchange of francs to the pound sterling at par is quoted as 25 francs 25 centimes. That would be the rate at which the actual coins would always exchange, except for a small commission charged by the money-changers, unless under exceptional conditions of stress or panic.

Let us now suppose for a moment that a number of bills on New York available for disposal in London are on the point of maturing—*i.e.*, due for payment—aggregating to a total of £100,000. Assume further that a number of British merchants are faced with having to meet on a given

date bills drawn against them by merchants in the United States for exactly the same amount. Then, other conditions being equal, the bills on New York will sell at what is the "par" between sterling and dollars (in gold), except, perhaps, for a very small broker's commission. The exchange with New York will then be said to be at par. But suppose that there are bills on New York for only £90,000 or £80,000, then the competitive bidding to buy the bills will raise them to a premium, which, however, cannot exceed the cost of sending gold, as is obvious. It is then said that the exchange with New York is against us. If, on the contrary, bills on New York exceed in amount the sum owing by British merchants to the United States, then the price will go to a discount. It is then said that the exchange with New York is in our favour. The buying and selling of bills on all trade centres throughout the world is going on daily and hourly—more so by far in London than in any other commercial centre in the world—and the price paid for the bills is expressed in the phrase so often seen, that "the exchanges are in our favour," or that "the exchanges are against us." It is called that because the quotations are always in terms of the currency exchange. Thus, for example, the par of the United States dollar being 4·82 to the sovereign, if the exchange on the United States is against us, the premium will be expressed by quoting the exchange of the dollar at a rise—say 4·76 to the sovereign—and when the exchange is in our favour it will be quoted at a fall from par, say 4·88 to the sovereign.

The main cause—indeed, the only cause when correctly interpreted, and as applying to bills representing actual transactions—of the disparity in the value of bills available at a given time between two countries is the fairly obvious one that the country on which there is an excess of bills

has been importing more from the country on which there is a deficiency of bills than it had exported to that country. Hence there is a balance remaining to pay which can only be met either by sending gold, by extending the time of credit, or by some other mercantile or banking contrivance which we shall see in a moment.

We have just said that, correctly interpreted, the fact that there is an excess of trade bills on one country proves that that country must have imported more than it had exported. The correctness of the interpretation depends upon a true appreciation of what should be included in imports and exports. Thus, England may be holding bills on the United States—it nearly always does—representing the earnings of her ships in carrying American freights. England has exported services—just what all production consists of on final analysis. The bills drawn against these services are finally liquidated in American goods, which appear on our Board of Trade records as imports apparently in excess of exports, and are so understood by people who do not know the subject, and who thus imagine that we get denuded of our gold to pay for this excess. Again, England may have been buying American stocks and shares; or it may have subscribed largely to new public or private loans. Against these purchases or subscriptions Americans will draw bills on England, to be employed in meeting accounts due to England for goods delivered or services rendered. England has imported paper claims on the future earnings of the American people, for which it pays by present exports, thus appearing to have exported more than she imported. Or the bills may be drawn against interest coupons held by British investors in American public loans and private enterprises—exports due from America in return for imports rendered by way of subscription to past loans.

In these and other ways bills will represent debts for what really amount to exports, though they may not so appear on Board of Trade lists.

The rate of exchange, then, is both a result and an index of the excess of imports by the country on which the exchange is "unfavourable," and *vice versa*. Other causes which influence the exchanges we shall come to presently. But before we get to that, we must examine a little further the machinery which the mercantile world has evolved for obviating the necessity of exporting and importing gold in payment of balances which are bound to arise, both in the occasional appreciable difference between exports and imports due to seasonal and other causes, and such habitual differences as there may be between two given countries one of which regularly imports more from the other than it exports to it. Thus, for example, the countries which are chiefly agricultural will naturally have an excess of exports during the autumn, but an excess of imports during the spring, when they are importing agricultural machinery and implements, materials for building and repairs, and many other things. But as regards such countries between which there is a regular disproportion between imports and exports, except for the adjustment of the difference in some other way, this could not really happen for any length of time. A nation can only buy as much of the products of other nations as it can pay for by its own products. Only the country which has gold-mines can buy for gold. All the other nations have first to buy the gold in exchange for their products, before they can hand it over in exchange for products to others; so that in the end it can only be products which buy products—in other words, the products get bartered in a roundabout way. The gold that is used in payments only duplicates the process, entailing a corresponding tax upon the gold

users, since the utilities for the maintenance of all those employed, directly and indirectly, in the gold production must of necessity be created by the gold users ; the share which falls to the gold producers being embodied in the value of the final commodities in the production of which the gold is made to co-operate as a factor, for which the consumer has then to give a full equivalent.

But how is this habitual difference between the exports and imports of two given countries to be adjusted ? Why, that is fairly obvious. If country A imports in the course of the year ten millions' worth more from country B than it exports to it, but, on the other hand, it exports ten millions' worth more to country C than it imports from it, all it need do is to transfer its surplus claims for ten millions on country C to its creditors in country B, and thus settle its indebtedness : directly by means of a bill of exchange currency—but indirectly and finally by paying for the imports by exports. This is what takes place in effect ; but the process by which it is accomplished will require some further elucidation.

Before bills can come effectively into play to take the place of gold in adjusting exchanges, it has been found in practice that there must be certain "centres" or "Exchanges." Now, everyone knows what an exchange is—for instance, the Corn Exchange, Wool Exchange, Coal Exchange, Stock Exchange, and many others—places where merchants and dealers meet to do certain classes of business. The question whether all these Exchanges, or the particular type of organisation, serve the purpose of industrial development most efficiently will be considered at a later stage. It will, however, be readily granted that it is, for example, much easier to buy or rent a house with the help of a house agent than walk miles of streets at random in the hope of coming across what one wants. It

is certainly difficult to imagine how buyers and sellers of bills are to be brought together, how the bills are to be found in sufficient variety of places, dates, and amounts, how the buyer is to decide as to the reliability he can place on the drawer and acceptor of the bill, without a well-known business centre where their collection and disposal is a recognised and well-organised enterprise. Curiously, though spoken of as an "exchange," there is really no actual "bill exchange," any more than there is an actual money "market." The foreign bill business in this country is done practically wholly in London by a number of well-known firms, some doing business on a very large scale indeed.

To convert our hypothetical countries A, B, and C, into concrete realities, let them be respectively the United States, China, and England. The United States exports little to China, but imports a great deal of her tea, silks, and other goods. To send gold regularly from America to China in payment of balances is out of the question. But the United States sells more to England (when the bonds and shares representing British investments in United States enterprises are included in her exports) than it buys from England. Hence it can pay China with bills on England due for balances of exports over imports ; and England then squares the account by exporting more to China than she imports thence, as she actually does in the vast quantity of cotton goods. Thus, between the three countries named an exact equation may be established between exports and imports, though any two of them will show a balance this way and that.

The process, however, by which this is accomplished becomes highly elaborated, and to those outside appears exceedingly complicated, owing mainly to the fact, just explained, that bill-dealing can only be carried through

efficiently from a well-organised centre of specialists who have given years of study to it, and each member of whom serves an apprenticeship to the business. Instead of three parties to the transaction—*i.e.*, the exporting and importing merchants in the three countries named, who establish the equilibrium between exports and imports—a fourth party steps in, in the form of a London bill-broker or what is called an “accepting house.” Thus, when the Chinese merchant sends his tea or silks to the United States, instead of drawing a bill on his American buyer, he draws it on a London firm on account of the American importer, a document accompanying the bill showing against what goods exported the bill is drawn. The Chinese merchant then gets paid in his own country by selling the bill on London to someone who wants it for settling an account in Great Britain for goods imported. The right of payment on a bill passes to the holder by endorsement of the drawer, and so on through subsequent endorsements. The accepting house in London then pay the amount to the merchant here who holds the credit on China for the goods exported, and themselves look to the American importer of the China tea or silks for payment on maturity, earning a commission or discount in the process. These bills, in turn, will then be met either by sale to British merchants who want to send them to America to meet liabilities there, or against bills on English merchants received here from America, due for goods imported into this country.

There is another kind of bill on which a few words must be said. This bill is known in home trading as an “accommodation” bill, and in foreign trading as a bill “drawn in blank.” An accommodation bill is a bill representing no actual business transaction, and in which, instead of the acceptor being in debt to the drawer, it is

the drawer who makes himself liable to the acceptor for the amount of the bill. The name of one merchant may be good for credit with his banker or in the open market, while another merchant who is known to the former, and whose position may be perfectly sound, is nevertheless not sufficiently known in the mercantile world for his paper to be readily discounted at the ordinary rate. It may be that the latter can give good security, though not of a kind that would be accepted by banks or discount firms, on account of not being readily saleable in the open market. The merchant, then, whose credit is good will, for a consideration, “accept” a bill drawn by the other, making himself liable to any subsequent holder of it, and the drawer then discounts the bill in the usual way, and uses the bank credit so raised in his business. This kind of bill may be regularly renewed over and over again, as each one is met by the payment of the drawer of the bill ; really amounting to a loan on the part of the acceptor, except that, instead of reducing his banking credit by the amount loaned, he lends only the use of his name (including liability in case of the drawer's failure), on which others advance the actual credit on payment of a discount. The mercantile world is partial to joint-responsibility paper, it being an obvious conclusion that where the debt rests severally between two or more persons, either of whom can be made liable, the risk is much lessened. Thus, in the case of a bill passed through several hands by endorsement, the holder must first present it on maturity to the acceptor ; and if he fails to pay, he can come down on the preceding endorser from whom he took the bill ; and if he also fails, the drawer is finally liable. If the endorser pays, then he, in turn, has his remedy against the previous endorser or against the drawer. A bill is merely a credit passed on, but not a

legal tender in settlement. A foreign "accommodation" bill will be drawn by a merchant in one country on a merchant in another country; or the accommodation may be given by a banker, on security. Banks and discount houses do not, in a general way, look upon accommodation paper with the same favour as on bills representing actual sales and despatch of goods; and such is claimed to be the knowledge and experience of the bill discounters regarding the position and doings of the mercantile world that they can generally tell an accommodation from an actual-transaction bill—mainly, I take it, from the knowledge that the names of the drawer and acceptor do not stand to each other in the relation of buyer and seller.

There is yet another kind of bill, somewhat analogous to the above, yet of a considerably different complexion. These bills are created in the case of those countries whose export and import periods do not coincide, to which reference has already been made. At a certain period of the year, Virginia, U.S.A., for example, will export much tobacco and raw cotton; but her imports are either distributed more evenly or come chiefly at a different period. Without some financial contrivance to meet the case, there would be a heavy balance to come to Virginia in her exporting season which would have to be paid in gold; and then at other times of the year, when she has no exports with which to pay for her imports, the gold would have to go back to the countries who paid it to her for the tobacco and cotton, to pay for the imports—a second transmission of gold with its attendant expenses, to say nothing of gold becoming dearer through its increased use. This difficulty is met at the time when bills on foreign merchants representing actual transactions are not to be had, by the Virginian bankers drawing, on account of their clients, bills on Continental bankers,

chiefly London, which can be used for transmission in payment of the excess of imports; and by the time these bills mature for payment (note that it is the drawers of the bills who are actually indebted) the Virginian exports are leaving the country, and the bills drawn on Continental merchants against the tobacco and cotton can then be sent to meet the accommodation acceptances given by the Continental bankers. And so by one contrivance and another the use of gold is economised, and its place taken by a paper currency to the proportion, probably, of some 200 to 1.

There are other causes of fluctuation in foreign exchanges besides what we know as "the balance of trade." One of these is the fluctuation in the ratio of value between the two metals in the case of countries one of which has a gold and the other a silver standard. When, for instance, the value of silver has fallen from 25 to 24 pence per ounce, the value of the bill payable in silver will naturally fall in relation to payment in gold. Of the other causes, only one more concerns us intimately, and this need not detain us for more than a sentence or two at this stage; for while it is a subject of the most vital importance to the currency problem, we shall get our grasp of it as we develop our subject to its completion. This cause of fluctuation in the exchanges hinges on the good credit and probable stability of the country on which the bills are drawn. If the Government of the country cannot be fully relied upon to honour its obligations; if there is more or less of commercial or financial stress or panic; if its paper currency is convertible, or its metallic currency is debased, so that there is no certainty what the face value of the bill will ultimately realise when it is converted in the end into the real value of goods or services; if the country is at war, or there is civil war, or if it is thought that either of these

is inevitable—any cause, in short, which gives some ground for doubting whether the country in its collective capacity as a Government, or its merchants and traders individually, will be able to render an equivalent for value received affects the rate of exchange between the respective countries.

CHAPTER XV*

THE CURRENCY PROBLEM—HOW WARS ARE PROVISIONED

THE economic structure, like an individual organism, may be said to consist, firstly, of a skeleton framework as a basis for supporting the tissues and organs, and, secondly, of a nervous system which keeps the organs and tissues in healthy working condition. By a vast network of arteries, veins, and capillaries, the world organism is employed in contributing a continuous supply of life-preserving utilities to a mighty stream, from which these are distributed to the multitude of units. But the means by which this distribution is accomplished consists of a nervous system of credits, manipulated by a composite substance of nerve tissues, made up of various credit instruments, worked and controlled from certain ganglia, or nerve centres—always highly sensitive, as is the nature of a nervous system, and subject to breakdowns, not alone from physical derangement of the tissues generally, but also from mental affections, which react on the nervous system.

The most important thing we have to grasp is the nature of credit, and what are the primary conditions necessary to keep it in healthy working efficiency. Well, I can fancy the reader saying, credit, of course, is lending something to somebody which he promises to repay. Quite so ; and

* This chapter has been partly rewritten, as a consequence of the war, for reasons which will be apparent. Otherwise the book remains as it was ready for publication before the war began.

provided each credit represents something lent, nothing much is likely to go wrong unless under very exceptional conditions of mental strain. For every credit which creates a claim, or right, to receive some utility there must be a corresponding debt of some utility having been given up, to be consumed by anyone who has a rightful demand upon it. So long as credits are of that character, we have the first and most important condition to a sound economic organism.

But let us get a little further insight into the matter. Economic progress is conditioned by the creation of surplus wealth (p. 103), which becomes available for the maintenance of those who are set to creating capital, by means of which production will be facilitated and made more prolific. In absence of a surplus there is economic stagnation; saving, in a word, is the very life-essence of economic advance. The contribution of that surplus wealth constitutes a debt, in return for which the rightful claimant—whether he actually created it or not is not material to the issue—holds a credit on future production. With the creation of these credits, and the invention of some instrument by which they can be transferred from one to another, a nervous system is set up whereby products get distributed; men forget the substance for which the credit stands, concentrate their mental energies on securing as much of these credit instruments as they possibly can, and a vast system of manipulation grows up—centres from which the nerve filaments radiate in all directions. But whatever the manipulation, each credit is the counterpart of a debit—one is entitled to receive because an equivalent has already been given up. So long as credits are wholly of that type the world over, nothing is likely to go wrong for any length of time; and it matters little what the instrument is which is used for passing on the credit from hand to hand. True,

panic plays some curious pranks with the human mind, and the most perfect economic machine may get out of gear under mental stress; but where each credit has a *bona-fide* debit behind it, it will soon be adjusted, with little, if any, damage. The system, then, functions efficiently because of its completely reciprocal character. All of us are aware that we are consuming utilities which have been created by hands no longer in the land of the living—if not in the houses we live in, certainly in the roads and railways we travel on, and in the land from which we draw our food, made cultivable and fertile by past generations. In return, some of that which we are creating to-day will be consumed by future generations.

On the other hand, where credits do not represent real debits, unless the utmost care is exercised by vigilant and experienced minds to see that they are created only for short periods for definite contingencies, to meet debits which are on the way to maturity, the mechanism is absolutely bound to go wrong once that kind of credit is set going. A claim is created on the stream of production when no equivalent has been put there; and scarcely anything can be more certain than that, once such a mechanism is admitted into the economic structure as a matter of course, a collapse is inevitable. I want the reader to be quite clear on this point. It is not enough to say: "I hold a credit, though nothing has been given up by anybody as its equivalent; but I have good possessions or security." The security is good for a debt, but not for a credit. If someone holds a credit on me, then my security keeps him safe; but if I hold a credit on someone, it must be because something has been given up. The banker's "acceptances," though temporarily giving a credit to the "drawer," nevertheless make him really debtor to that amount. They are personal as between banker and client

(in the case of foreign acceptances the "drawer" is frequently also a banker), are nothing more than banker's loans, but are preferred to "overdrafts" because of their post-dated character. Such documents would become exceedingly dangerous if they were blank credits on the community in general, as we shall see before long.

Let us put it in yet another way, since the matter is of such vital importance to an understanding of the subject. The complicated system of a credit currency is nothing more than a highly elaborated contrivance to accomplish barter in a roundabout way, periods of more or less length intervening between the giving up and receiving a return. Without such a contrivance, subdivision and co-operation in production could not have taken place, and man must have remained abjectly poor, in his primal savagery. What this credit system does is that, instead of saying, "I give you this and you give me that," we now say, "I claim this as an agreed upon equivalent for something that has already been given up." In this way a claim on wealth is created as a result of an addition to the store of wealth. Only that is taken out which has already been put in. The bits of paper or coins by means of which the claims are enforced may, by some dishonest means, be filched from the rightful owners; but while this would inflict hardship upon individuals, from the economic standpoint of the producing structure it matters nothing whether the product is claimed by A or B, so long as it stands for a real debit—a contribution of wealth to the stream. You establish an economic equation as between contributions on the one side and withdrawals on the other side. But once you attempt to create credits which do not stand for actual debts, you are on the high road to economic perdition. You do not produce wealth by ringing the changes, whether you do it with coins or bits of paper, though that apparently is the

general impression. People see others getting rich by financial manipulations, and so come to attribute a sort of magic property for creating wealth to anything that is called money. But the manipulation is either a necessary part of the mechanism of exchange—in which case the high reward is a question of Exclusive Access—or it is simply a piece of clever chicanery for appropriating claims rightly belonging to others—in which case nothing whatever is added to the store of wealth. *Ex nihilo nihil fit.* A nought multiplied by a nought still remains nought. The history of finance furnishes examples of credit currencies of this character, accompanied by disastrous results; and at the time of writing this (September, 1915) we have another striking example of a similar credit currency, with which we shall deal presently.

Here the reader—whose critical faculty has by now, I trust, developed to razor keenness—will perhaps detect an apparent discrepancy. We have already made the proposition that, from a purely currency standpoint, it matters not one iota who provides the currency, and whatever in the world it consists of, so long as it commands acceptability, and there is no more of it than is just required to perform whatever happens to be the volume of exchanges at any time; the former being, apart from national upheaval or breakdown, really the consequence of the latter—*i.e.*, that acceptability, once it is established, will keep so, so long as the currency does not become redundant. But, the reader will object, is not this the very thing just condemned so energetically as a system of creating credits without debits behind them? Such an objection can only come through his having momentarily forgotten what production means in the economic sense. The provider of the currency, whoever he is, must be taken to have some special qualifications for the purpose

—what, to follow the terms of our unifying law, we should call Exclusive Access—otherwise it would not be left in his hands uncontested ; and given the acceptability and absence of redundancy, with the consequent efficiency of function, he has provided an indispensable tool without which the machine could not have been kept going. The real point in the condemnation of currency credits which represent no real debits is just this : that such tools are certain to cease functioning efficiently, as a consequence of becoming redundant. The provider of the plane, though he has no direct hand in the making of the cabinet, has nevertheless contributed to its making, since it could not have been made without the use of the tool. The cost of the tool—in economic reality the maintenance of the tool-maker—therefore forms an item in the price of the cabinet ; in other words, the consumer must give of his own products or services in exchange an equivalent of all the factors necessary to the creation of the cabinet. But supposing the cabinet-maker were to burden himself with a needless number of planes, the problem would then arise that the price of the cabinet must either include items for the maintenance of some parasitic hangers-on—the makers of the redundant planes—or someone will have to starve. We have already examined the forces which tend to redundancy, or “over-production,” and the consequences following from them. But while the disorganisation due to what is called “over-production” will be more or less limited to given industries, or, at any rate, tend to operate sectionally and unevenly, the “over-production” of the currency tool, owing to its being a general claim on wealth—an indispensable instrument in all industries alike—tends to a collapse of the economic fabric as a whole : the breakdown of the central power-station, as it were, from which the whole economic machinery draws its momentum. In

a word, then, the claims on wealth held by the providers of the currency represent real debits so long as the tool which they provide functions efficiently ; and it will only so function if it is not redundant. They become parasitic hangers-on to the extent that the tool has ceased to function efficiently. But since the failure of the currency tends to a general collapse, those responsible for it are something worse than mere parasites—they are the wreckers of the whole industrial structure of the nation.

It probably never occurs to one in a million that he pays for the use of the gold which he receives in payment for his services. One knows, of course, that a sovereign's worth of goods is not some fixed quantity, but just what can be got for it at a given time. What is not so clear is that the price of the goods contains added items, which the consumer pays, as a consequence of the employment of the currency which has become a necessary instrument. Translated into economic reality, that means that a part of the total products contributed to the stream will be appropriated for the maintenance of all those engaged, directly or indirectly, in the production of gold, in return for their co-operation in providing an instrument without which production could either not have been carried on at all, or not to the same extent. When in place of gold paper currency is employed, the item for the use of currency equally forms an added charge in the price of the commodity. The proceeds of the added charge now makes its way into the hands of those employed in the management of all the paper instruments. The nation as a whole does not escape having to provide for the maintenance of a number of people employed in creating currency instruments, whether they be mine-owners, diggers, smelters, refiners, transporters, bullion dealers or brokers, or whether they be bankers, accepting houses, bill brokers, and their

numerous staffs. In either case they are included in the circle of produce-consumers who hold claims on the total product, in return for services rendered. But there may be a considerable difference between the two in the matter of costs. If the number employed in the management of the paper currency is smaller than would have been necessary to employ in producing that much of gold, or if the service rendered in providing the paper currency is less highly rewarded, then the use of the paper currency is, to that extent, a national saving. The provision of paper currency, in which the cost of materials is negligible, is obviously much more susceptible of economy than the extraction of gold. In essence, the currency problem as presented to-day resolves itself into the question of how to economise the use of gold. This involves the secondary problem of how to avoid the danger of redundancy to which a non-commodity currency is obviously so much more liable than a rare commodity such as gold. Some, indeed, would put the problem higher than this, by asking if it is not possible to entirely dispense with the use of gold.

At first glance, it would seem that a commodity unit of value is as indispensable as a tangible, fixed unit of length or weight. How is one to know a money unit, it will be asked, whether you call it a pound, a dollar, a mark, or a franc, unless there is some agreed-upon, tangible substance of given weight and quality which has, at any rate, a fairly steady exchange value in the open market, even if it is kept only as a standard for verification? But this is really not so—there is no parallel whatever between a fixed unit of length or weight and a unit of value. No doubt if a country were to step direct from a condition of pure barter into the adoption of an ideal currency—paper or some other object of no commodity value—it would at first have

some difficulty in getting its citizens accustomed to compute readily the ratio of exchange between things. On our assumption of a State so highly developed intellectually as to be capable of a direct transition from pure barter to an ideal currency, we may take it that its paper-note unit would, at first, be based on a fixed unit of some highly prized commodity—probably a given measure of corn. Thus, a citizen giving up for the use of the State a measure of corn would receive a currency note for it, entitling him to draw from the stream of production anything which at the market rate exchanges for that measure of corn. The quantity obtainable of that something which he desires in exchange may be less a day, or week, or a month later than could have been obtained at the time; but in that respect he is no worse off than if he had received a metal coin, unless the change is due to a depreciation of the currency, which would have been avoided if it had been a commodity currency. Once a ratio is fairly established in terms of the currency unit, the original fixing of the value of the unit ceases to serve any real purpose. Unlike extension and mass, value of a thing is incapable of being expressed or conceived except as related to something else—by which one means, of course, economic value, not personal appreciation or desire. When you say that a certain thing is worth a sovereign, you express a ratio between the coin and the thing—indeed, you make a comparison between that thing and many other things which will exchange for as much, or more, or less. It matters nothing whether you express the comparisons in terms of bushels of corn, or Treasury notes, or imaginary macutes. The unit of value is an algebraic symbol which has to do, not with some given concrete quantity, but with relations of quantities to each other. The thing worth two units is always twice the value of that worth only one unit, whether the unit be a coin, an ox, or an abracadabra. So long as the

currency instrument functions, its substance or value, commodity or conventional, is of no consequence whatever.

By the time that a nation feels the need of a paper currency, it must have already developed a considerable trade with foreign countries; hence the world has really never had the experience requisite to test the efficiency of a currency for national exchanges alone, free from the difficulties and complications arising from international trading. If we suppose a self-contained country having no dealings whatever with the rest of the world, it is fairly safe to say that, given a stable national life, and the management of the currency on sound principles, a State currency consisting wholly of paper would be not only feasible, but both exceedingly economical and much more free from fluctuations than a commodity currency, which is liable to varying supply beyond the control of the State. Nor, indeed, is there any ground for saying that such a currency may not be a perfectly efficient instrument for international exchanges the world over at some future time, when wars shall have become a thing of the evil past, and national stability, solvency, and integrity, a firmly rooted condition of social life. But since such a consummation is yet in the distant future, we have to consider what is feasible under existing conditions. It is not, then, the question of a unit of value which necessitates the employment of a commodity currency. It becomes indispensable primarily as a result of international trading. So long as any one country employs metallic currency, and insists upon its contracts for payment being made in terms of that currency, the other nations are perforce bound to follow suit. If a nation, like Russia, for instance, adopts an almost complete paper currency for home circulation, it does not escape the necessity of keeping a large gold reserve to meet foreign trade liabilities, and for special emergencies—a much larger re-

serve, indeed, than a country like the United Kingdom, which uses much more gold in daily circulation.

In the ordinary course of trade, goods bought abroad are generally paid for by goods exported from home. Nevertheless, the seller is manifestly bound to stipulate for payment in the currency of his own country, for reasons which are too obvious to need stating. So long, therefore, as the debtor's country has a similar metallic currency (or keeps a stock of bullion, which comes to practically the same thing), should the contingency arise for paying in cash, the actual metals are always exchangeable at par, less a nominal commission (pp. 256, 274), so that the additional expense is only a question of freight and insurance in transit. But if the payment had to be accomplished by exchanging the currency paper of one's own country abroad for the metallic money of the creditor country, the very fact of the shortage of exports, which is the cause of the payments having to be made in cash, would send the paper currency down to a heavy discount. But even payment in gold, if continued for any length, sends the gold also to a discount, to the disadvantage of the creditor country—*i.e.*, it ceases to exchange for as much of commodities as it did before. Countries demand from each other products for consumption, not gold or repeated promises to pay. That is the purpose of trading from the national standpoint, however the individual trader may see it. But since a contract must necessarily stipulate for payment in some one thing—since it is obviously out of the question to leave the debtor the choice of paying in any one commodity that suits best his interest or convenience—gold is, for reasons already amply given, the best possible contract unit for payment of debts. Next to getting what the seller really does want, gold will most nearly insure the getting of an equivalent at some future date. Hence

the exigencies of contract and payments abroad impose practical compulsion on every commercial nation to have a metallic standard, and to keep a reserve of gold to meet probable emergencies. To a less extent, the same considerations apply to a contract unit for payments at home. True, the legislature can make notes legal tender. We shall have to deal presently at some length with the question of note issue. Meanwhile it is sufficient to say that, unless the notes are convertible into gold on demand, the enactment cannot prevent the paper going to a discount in face of causes which impair its acceptability. Though the seller may not refuse the legal tender note, he will take good care that, if payment in gold is not offered in advance, the price of the goods he is selling shall go up by so much per cent.

Granted, therefore, that a gold basis is an essential of modern currency under existing conditions, we have this threefold problem before us : (1) How broad is that basis to be—in other words, how far can the use of gold be economised with safety, by the substitution of a paper currency? (2) How is the paper issue to be regulated (a) so as to provide an ample currency for all national needs, while (b) at the same time avoiding the fatal error of over-issue? (3) Would not the issue of notes (a) function more efficiently, (b) run less risk of redundancy, and (c) be much more economical, if it were administered by the State, instead of being left in the hands of bankers? Added to which comes the still wider question, Should not the State undertake the business of banking, either as a State monopoly or side by side with other banks?

The paper currency is of several kinds. The greater proportion of it in this country is made up of cheques. These are entirely free from the danger of excess, as they do not remain in the channel of circulation, each cheque

being cancelled with the transaction to which it refers. In the history of currency there is scarcely anything more striking than the rapid development of the use of the cheque. Yet there is room for a much wider extension of its use by a system of banking which appealed more successfully to the petty tradesman, the well-remunerated mechanic, and people of small means generally. At present these either do not bank at all, or will only be induced to do so by an offer of high interest, often to their undoing. The cheque could be utilised for small payments much more extensively than it is at present. Next to the cheque come the mercantile bills. These have already been sufficiently dealt with in the preceding chapter. Then comes the note issue—the legal-tender currency—which forms by far the most difficult question in the currency problem. Before entering upon this final stage of our investigation of the currency problem, let us take a glance at the economic position as disclosed by the present war.

The devastating war in which the world is now plunged has just one tiny redeeming speck to its credit side. It is proving an economic educator of some consequence, both in evolving a clearer vision of economic conception, and, as a hard taskmaster, compelling obedience to economic law. The doctrine which we have done our best to demolish, that the production of luxuries—the creation of "useless frills"—is both the indispensable means of providing a livelihood for many workers and an integral part of the economic structure, without which the machine would break down, is at last receiving a shattering demolition beyond anything that my puny efforts could have accomplished. Daily we realise more and more the direct and intimate connection between production and consumption—that, e.g., producing scent for chows' cots is

not exactly the best way of getting boots for the army—that if you want boots you must make boots, or shells if you want shells. The journals which could see silver linings to the clouds of crime, and economic salvation in the production of frills for decorating the cutlet, are now falling over each other in their earnest endeavour to impress upon their readers the need of the most strenuous efforts in the production of necessities, abstention from consuming luxuries, and the practice of the most frugal economy. At last the Mercantile Theory of economics is getting an effective set-back. The "useless frills" theory of wealth production will not have so congenial a soil to flourish in as it had in the past.

And yet a great deal of the phraseology used in connection with providing the means for carrying on the war tends to undo much of that which the hard facts are gradually instilling into people's minds. As an example of how the "man in the street" understands it, here is how one newspaper puts it: "Nearly 600 millions in hard cash have been plumped down by the nation in order to crush Kaiserism and liberate Europe. Not paper, but yellow gold, every sovereign payable before the end of October." The reader will not need to be told how fantastic this notion is. I should be very much surprised indeed if one-twelfth of that sum in gold has been paid in in subscriptions to the loan.

The staggering figures of the cost of the war are indeed sufficient to perplex even the most hardened economist. Take our own case. The national income before the war, at its high-water mark, was estimated at about £2,400,000,000, of which about £300,000,000 was being invested abroad, while another £100,000,000 or so went to replace used-up plant at home. Thus the annual national consumption, apart from capital investment,

was somewhere about £2,000,000,000. Including loans to our allies, we have for some time been spending more than two millions per day, and at present (October, 1915) it is probably nearer five than three millions—in round figures, £1,600,000,000 a year. Before we have finished, the cost will probably rise higher than this. Where, then, it will be asked, is this gigantic sum to come from? If we take that much or more for carrying on the war, where is the fund for the maintenance of the nation to come from? True, the cost includes the maintenance of a large section of the nation—including the families of the married, probably considerably more than a third—consisting of the army, navy, and those engaged in war work of all kinds; but, on the other hand, the bulk of these have been withdrawn from productive employment, so that the national income is diminished to that extent. To such as the writer quoted above, who conceive the economic fabric in terms of "yellow gold," it is purely a question of employing the right methods to tapping the gold-supply. In old stockings and many other hiding-places the people of this country have a great store of gold hidden away, and it is only a question of how to make them give it up to the Government, whether by loan or by taxation. What gold we are short of we must borrow from the United States. Once the gold is there, the rest follows as a matter of course.

Unfortunately, even the informed writers are contributing largely to encouraging this delusion. Certainly, the statement of economic problems in terms of money is an exceedingly convenient economic shorthand, as it were. Provided it may be taken for granted that the reader understands the vicarious character of the money terms, it is an admirable medium for stating the case quantitatively in a very few words, as compared with

having to state it in terms of products and services; while, at the same time, if viewed merely as necessary machinery, and provided the term "money" is understood to stand for all currency instruments, it expresses the case accurately enough. The drawback is that you cannot take it for granted that the reader understands the interpretation and qualifications; indeed, you can safely take the exact opposite for granted—that he will understand it literally as a problem of getting so much gold. I came across striking illustrations recently in separate conversations with two gentlemen, one a cute City man and the other a large employer of labour. Speaking of the destruction of wealth, each said in similar words: "Oh, I don't think so much of that—the money is not destroyed." There you have it in a nutshell.

At the risk of tiresome iteration, we may venture to investigate as briefly as possible the part which the money factor performs in the process. To some extent, the actual gold or bullion contained within the country at the beginning of the war may be exchanged for supplies abroad; but this is really so contemptible an item in the enormous total that to talk of gold as the chief provision for carrying on the war is sheer puerility. Yet, as a steady element, a reserve of gold plays an extremely important part; and it does so for the very reason that the neutral countries from which we obtain supplies do not want the gold. The reader will remember that before the war one had to pay more for exchanging gold than paper in many Continental cities. The banker did not want the gold; it simply had to be sent back to London, the gold-market of the world. They want goods—things for consumption, not merely claims on things—but in the last resort, being a commodity as well as the basic element of currency, gold is the next best payment—at any rate,

it seems the only possible contract unit. Did they really want gold, the well would run dry in a few days, and the walls crumble into fine powder. The fact that the gold is there inspires confidence, and occasionally it is used for payments; but in amounts small to insignificance comparable to the mighty total. Our Bank of England reserve at the highest since the war began stood at £72,000,000.

When a private individual finds himself faced with an additional heavy expense—say an illness in the family—he will endeavour to meet it in one or all of the following several ways: (1) He may be able to pay for it out of current income by using up the surplus hitherto put aside for saving; (2) or he may pay for it out of past savings; (3) or he may economise in his ordinary expenses, forgoing many a luxury and comfort to which he has been accustomed, thus leaving a surplus for doctor's bills, drugs, and sick-room comforts; (4) or he may obtain employment additional to his ordinary daily occupation; (5) or he may borrow; (6) or he may send out his children, whom he would have preferred to keep at school or at home, to supplement his own earnings. If the case is serious and prolonged, he may have to employ all of these means. Some of these are obviously susceptible of varying degrees. The economising may border on penury; the additional labour may be prolonged and arduous; the borrowing may be any amount which he can induce lenders to grant; the children—boys, girls, or both—may be put to work at various ages.

It is exactly the same in the case of a nation, except that some of the terms must be understood in the national sense, which frequently differs considerably from the sense in which they are applicable to individuals. With this the reader is already familiar. The past savings

which a nation can consume in provisioning a war are the "real" savings, not the "personal" savings (p. 77 *et seq.*), but including investments abroad. Thus, it may consume its live-stock, its metals, its accumulated raw materials of many kinds, its public buildings, its railways and shipping, without replacing them or keeping them in good repair; and it may sell its foreign securities. It is then consuming the nation's capital. The "personal" savings, though contributed to the State by taxation or loan, are nothing but the machinery whereby current production is put at the service of the State, as we shall see in a moment. Again, provisioning by national borrowing means only borrowing from abroad. When a State borrows at home, it is simply adopting one of two available methods for appropriating to its use (a) past "real" savings, and (b) current income.

The "financing" is merely the contrivance or machinery whereby the State is (1) given the claims on, and (2) the power of directing labour to the production of, those things which are necessary for carrying on the war. Whether it is raised by taxation or by loan, it is simply a question of (a) compelling or (b) inducing the production of surplus wealth (p. 103) of the kind requisite for the prosecution of the war. A farmer or boot manufacturer subscribes to the war loan by a cheque on his bankers, and so much of his credit is transferred to the Treasury account at another bank, his own account being debited to a like amount. To meet that debit, a surplus of farm produce, or of so many pairs of boots, will be at the disposal of the Treasury, who will have to refund an equivalent of credit in payment, which will go to replace the credit of the farmer or bootmaker. The replaced credit will then be available for paying the second instalment of the loan subscription, once more placing farm produce or boots

at the disposal of the Government, and so on. What has been subscribed is so much farm produce, or so many pairs of boots, and but very few "yellow sovereigns" indeed. One citizen denies himself his usual summer suit, another forgoes his customary holiday, and a third economises so much a week on his household expenses. Each subscribes to the war loan, and experiences the satisfaction of having provided so many "silver bullets" —so much gold saved and lent to the State. In actual fact, what takes place is that the labour which would have gone to produce tweed for the summer suit is diverted to making khaki and blue serge for clothing our soldiers and sailors; that the food and services which would have been consumed by the others is diverted to be consumed by our army and navy, or by the workers who are set to producing munitions.

On the one hand, the money credits, in whatever form, represent so much of utilities contributed to the stream of production; and, on the other hand, the transference of those credits enable the State to use the utilities for the maintenance of those who are engaged in doing the nation's fighting, or in providing stores and munitions. The loan subscribers deny themselves some luxury or comfort for which the utilities which they have provided could have been exchanged; and the erstwhile luxury or comfort providers, being without occupation owing to the lessened demand, must now turn their hand to the making of stores or munitions in order to obtain the claims on the utilities necessary for their subsistence. It is a matter not alone of creating surplus wealth, but of so directing production that the wealth shall consist of just those things which are necessary for the purpose in hand. We are driven by the inexorable logic of hard necessity to realise that the production of things which, in terms of the

market, have a money value is by no means the same thing as producing that which is needed in given conditions.

It is this fallacy of conceiving the cost of a war to be a question of so much money that is responsible for the deplorable blunder so widely prevalent in this country at the beginning of the war, which counted upon an early breakdown of Germany for lack of money. It has long been a puzzling problem how poor nations, *e.g.*, like the Balkan States, managed to carry on an expensive war for a couple of years, when, if they had any decent respect for prevalent economic vision, they should have broken down in a few months. Yet no warning was taken from these glaring examples to discard the economic crudity that the cost of a thing meant the providing of an equivalent amount of gold. Did the Panama Canal cost 70 millions? Then the United States must have saved up 70 millions in gold to pay for it. Is a war to cost 3,000 millions? Then the nation must somehow raise a sum of 3,000 millions. But the United States did not save up 70 millions to pay for the Canal; it probably saved nothing at all in advance. It paid for it week by week and year by year out of current income, and that not in gold. In economic reality, a great number of citizens were producing day by day more than they were consuming, thus leaving a surplus to be consumed by those who were giving their services to build the Canal. The few coins, greenbacks, and other forms of currency circulating weekly between the wage and salary earners and the banks, were simply the financial machinery for dealing with the surplus. The taxation—if there was a special tax for the purpose—or loan was simply the means of inducing the creation of the surplus, and of draining it into the right channel.

But surplus wealth, as the reader knows, does not mean something left over after the producer thereof has fully satisfied his desires. It is very doubtful indeed if, on these terms, there would ever have been any surplus—in which case the human race must have remained in its primitive savagery. It is quite impossible to form any estimate whatever of the surplus that a nation is capable of producing. It depends, as already stated, on five different factors—apart from borrowing abroad—three of which are of quite unknown dimensions. But a nation may neither have the inclination nor the apparent need to bring the exceptional factors into play for the purpose of building a canal. In times of peace, the economist is quite on safe ground in estimating a nation's income by its habitual productive capacity, just as the actuary is safe in estimating the duration of life in normal conditions. But just as an epidemic will upset the actuary's calculation, the imperative needs of war will bring dormant factors into play to compel economy on the one hand, and to increase production on the other. A section of the nation, some wholly non-productive, and others engaged in promoting social changes which may or may not prove beneficial, are drawn into the circle of producers. Capital is probably being destroyed, education neglected, social movements of consequence put in abeyance; but the insatiable Moloch of war insistently exacts its due. In Germany much consideration has also been given to finding new uses for natural products hitherto thought unfit for human consumption, and to the preparation of other products in a way that will make them nutritious and palatable. Effective organisation and co-ordination of parts also counts for a great deal—for much more, indeed, than people in this country can yet be made to realise. Of this we have recently become painfully

conscious in regard to the production of munitions, which has proved so lamentable a failure while it was entrusted to the individual initiative of manufacturers; but few of us have as yet had the good sense to apply this severe lesson to the whole field of national enterprise. Agricultural countries, though relatively poor in normal times, have greater staying-powers in war-time. As between two industrial countries, on the one hand, the country which has its agricultural industry more highly developed will have a considerable advantage; and, on the other hand, the one which is more effectually shut off from trading with the rest of the world is bound to feel the pinch much sooner and much more severely. But while this may well prove the determining factor in the present war, the process of exhaustion is much slower than people were led to believe.

Financing a war by means of internal loans is generally looked upon as shifting on the burden to future generations. Put in this way, the statement is largely misleading. Apart from using up accumulated wealth and of borrowing abroad, the burden can only be borne by the contemporaries, whose products and services are the only available means for carrying on the war. What the interest on the loan does is to bind future generations to compensate the descendants of those who have borne the brunt for the sacrifices made by their ancestors. Provided the war is a just one—a view held by all nations at war, though the future may pronounce a different verdict—and apart from incidence, I can see no particular injustice in this, as the welfare of future generations must necessarily be involved in the outcome of a war. But very frequently the unjust incidence takes all the virtue out of this argument. Conceivably, the class which is advancing the loan may be the same class which is providing

by means of an income-tax the interest on the loan, in which case they will be paying interest to themselves. When the loan capital is repayable at some future date, if the sinking-fund is created out of the same taxes, then the bondholders are themselves redeeming their bonds. But if the interest is paid out of indirect taxation levied mainly on articles of necessity, then the bulk of the burden will fall upon the poorer classes, who will have to pay toll to a rentier class for a sacrifice (perhaps little missed) made by their well-to-do ancestors.

Let us put the matter into some concrete shape by way of illustration. In round figures, there were some 13 million persons engaged in occupations in the United Kingdom at the last census. These produced between them an income of 2,400 millions—say an average of £185 for each producer—of which 2,000 millions was consumed at home. Let us suppose that half of these workers have been withdrawn from productive occupations. That would leave us 800 millions short of our maintenance fund, leaving out the few hundred millions previously given up to investing abroad. To that has to be added loans to our allies and colonies—say 400 millions—making a total shortage of 1,200 millions. How is this to be made good? Suppose, then, that the whole nation economises in its consumption by one-third (on an average). That would account for 666 millions. Suppose, further, that 2 millions of those previously unoccupied joined the ranks of producers. That would account for a further 370 millions. We will suppose, further, that these 8½ millions now employed, by working longer hours and more strenuously, increase their productive capacity by one-tenth. That would provide a further 140 millions. Our account would then stand thus:

Shortage owing to cessation of production	£1,200,000,000
Less economy in consumption	£666,000,000
Increased productivity	£40,000,000
Idlers turned into producers	£370,000,000
	<u>£1,176,000,000</u>
Adverse balance	£24,000,000

There is, of course, no pretence to accuracy in these figures. Many factors have to be taken into account and allowed for. Thus, while the rich could well economise more than one-third, others are scarcely in a position to economise at all, while the maintenance of the new army, navy, and munition workers is on a distinctly more generous scale than fell to their share in industrial life. Then the term "economy" must be correctly interpreted, and it will then be found that not all that is economised is divertible to a maintenance fund. Like all else stated in money terms, it is open to an entirely wrong conception. By reducing consumption you will save money (assuming you have it to spend), but if at the same time you reduce your production of necessities by an equal quantity, such economy adds nothing to the maintenance fund. The economy must be that which results in a surplus of the right kind—something produced more than is being consumed, and so remaining available to be consumed by others. The idler who receives an income from other sources—rent, dividends, and so on—who economises and pays the money so saved in taxes, or subscribes it to a loan, simply transfers the claims on the products which make up his rent or dividend—he leaves that which he might have consumed himself as a surplus to be consumed by others, and frequently the nature of the

surplus is changed by the fact that he has ceased to demand a certain class of goods. In the main, the whole problem of economising resolves itself into a cessation of luxury production, or goods to pay for imported luxuries, and the utilisation of the energy so saved to the production of necessities, or goods that are changed for necessities abroad. But not all the energy or earning capacity so saved is divertible to the new needs. The artist who is capable of producing a picture which used to sell for three figures is not likely to produce as much if put to factory or farm work. The jeweller is likely to make but a poor dock hand or munition worker. Some considerable part of the national income will be lost by lack of adaptability. On the other hand, something quite appreciable may be gained by better organisation and co-ordination. We have no data for estimating what can be added by increasing the hours of work. It by no means follows that the addition of two hours to the miner's or engineer's working day of eight hours will mean an increase of product by one-fourth—certainly not for any length of time. While, then, we are not in a position to get at precise figures, our calculation presents accurately enough the nature of the problem we have to face. If the reader will entirely discard the use of the "pound sterling" term, and substitute for it the term "unit of product" (taken to be of an equal exchange value to the pound sterling), he will get a much truer vision of the economic reality behind the money terms. Conceivably, an absolute despot could dragoon his slave subjects into the requisite services without the slightest need of what we know as financing (though it is scarcely to be conceived that either the fighting or producing capacity could equal that of a people imbued with a sense of freedom). In absence of such despotic powers, nations have to resort to the art of

financing—the machinery which is at the same time the means of putting on the necessary pressure and inducement to the production of the requisite surplus to be placed at the service of the State, and the tool which is used for handling and directing the various goods and services to their proper destinations.

There is no question, of course, of improvising a brand-new financial machine as a consequence of being at war. The main structure has been fashioned and elaborated during many centuries. Yet the staggering magnitude of the present war makes the difference in the financial problem almost one of kind rather than of degree. It is one thing to devise taxes and loans of sufficient pressure and inducement to drain the normal surplus and to compel moderate economy, but quite another thing to make the pressure sufficient to bring about the results we have just analysed. One must always remember that problems in finance are at the same time problems in psychology. The man who subscribes £1,000 to a war loan, and subsequently pays the interest to himself and provides the redemption fund, does not see it in that light. He feels the satisfaction of earning interest on loaned capital which is coming back, whereas he would feel a heavy tax of the kind an intolerable exaction, amounting to confiscation. A machine is a contrivance for utilising some natural force, but the force may prove to be highly destructive instead of beneficial if the machine is badly constructed or imperfectly adjusted. This applies with vastly greater cogency to the financial machine, in which the natural force to be utilised—the producing capacity of the units composing the nation—consists largely of mental force, which may be affected disastrously not alone by unjust taxation, but even by taxation which, though ethically most equitable, should meet with strong antagonism.

National financing has many possible devices and contrivances, but each must scrupulously avoid the danger of upsetting the mental balance—the confidence which is the very life of the credit system controlling modern production.

The sound principle underlying all financing devices has already been dealt with, but let us put it into some concrete shape. We will suppose a country in which the citizens have deposits at their bankers, over and above the minimum necessary for carrying on the nation's industry, amounting to 400 millions sterling. These represent savings—surplus products contributed to the stream of production. The Government induces the depositors to transfer the credits to the national Treasury by way of loan. That credit is then used to drain from the stream that class of goods which is required for prosecuting the war. An increased demand is created for that class of goods, and a corresponding diminution of demand for other classes of goods, which might otherwise have been obtained by these very credits, lent out by the bankers in the ordinary course of their business. The manufacturing producers hasten to fill up the gap made by the increased demand. Meanwhile the credits transferred to the Treasury dribble back to the producers in payment of the goods demanded. In course of time, the credits get back into the hands of those who are in a position to save, and are once more deposited in the banks. This means that a fresh surplus has been created. They are not the old credits over again; they are new credits created by virtue of new wealth having been contributed to the stream of production. The Government may then issue a second loan, and once more drain the newly created wealth; and the process may be repeated as many times as is necessary, so long as the country is capable of producing

the requisite wealth. This, in brief, is the only sound principle of financing, whatever forms the loans may take. It is not a matter of juggling with credits, paper, or gold; it is purely a matter of getting the citizens to produce, and to continue producing, a surplus of those products which are required, and to give them up for the use of the State. The art of financing them consists in making the inducement just sufficiently attractive, and in employing the right agents and methods to carry the loans through successfully. That alone, however, may not suffice. It is probable that before we have gone through with the war a forced loan will be found indispensable.

It is not my province to preach homilies—mine is a much humbler task. Yet, as this book may get into the hands of some readers long before the war is concluded, I feel that I should not be doing my duty as a citizen if I failed to emphasise the imperative need for the most rigid, parsimonious economy. I am bound to say that as yet the bulk of the nation do not realise it—at any rate, they do not practise it as they should. Indeed, I have come across some who are still obsessed by that baneful economic counterfeit that “it makes money circulate.” When will people be made to see the senseless fatuity of that wretched imposture which has debased the economic currency for so long !

There is, however, the apparently easy method of financing by the issue of *inconvertible notes*, which few States at war are able to resist. The quantity of notes required in relation to the volume of exchanges will, amongst other causes, depend upon the extent to which other instruments of exchange are occupying the channel. Thus, a scarcity of gold, and a contraction in the use of

mercantile paper and of credit generally, will give scope to a proportionately larger note circulation. Hence, in time of war there is always room for a considerably larger note issue. The Bank of England note circulation in July averaged 33 millions, as against 26 millions in July, 1914; and in addition to that, 100 millions in Treasury Notes have now been issued, nearly the whole of which are in circulation—in round figures, an addition to the currency of fully 100 millions. As probably that much in gold has been withdrawn from circulation, the issue is by no means excessive. As against this, Germany has increased her note circulation by no less than 193 millions, with a total issue of 303 millions, and France has increased hers by 219 million, with a total issue of 456 millions. But as regards the latter, it must be borne in mind that France has long had a large note circulation, the amount in 1914 being 237 millions, against 110 millions in Germany, and only 26 millions in this country. In France, and to a much smaller extent in Germany, the note largely held the place which cheques hold in this country.

Germany's method of raising her war loans differs in at least one most essential respect from ours. We have so far adopted the sound plan outlined above. The available credit balance being insufficient for this purpose, Germany has adopted what is practically a copy of the disastrous experiment made in France by John Law. In addition to the State Bank and the established Loan Banks and the Mortgage Banks, other credit institutions were started, notably the War-credit Banks, spread all over the country. The Loan Banks can only make advances on a certain type of security, but the other banks can lend on mortgage, or on practically any kind of security, including even personal credit. There is also an Insurance Bank, which advances 40 per cent. on the value of life policies. The

people are not only encouraged to borrow from these banks in order to subscribe to the war loans, but much social and financial pressure is exercised to make them do so. The banks are authorised to issue notes on the strength of these mortgage and other securities, and the State Bank can, in its turn, issue its own notes, now inconvertible, against the notes so created by the other banks, which are paid in as subscriptions to war loans. In effect, then, the State Bank is issuing notes backed by the property owned by the people, pledged to the various banks as security for repayment. The issue of notes by the Loan and Mortgage Banks was at first limited to 70 millions, but has since been gradually expanded, until we get the result we see now. Theoretically, an issue of notes on this basis is only limited by the total value of the whole of the nation's assets, less only by whatever may be fixed as the safety-margin in granting the loans—say to three-fourths or two-thirds of the value.

Now, the vital distinction between a subscription out of savings and that out of a credit artificially created against a mortgage is this: that whereas the bank credit stands for an actual surplus contributed and made available for consumption by whoever gets possession of the credit constituting the valid claim on that surplus, the subscription made out of a credit manufactured simply by means of a copperplate and printing press—however good the security—stands for nothing at all. The mortgaged property is in use by the owner, and even if you were to take it away from him to be consumed by others, you would be merely robbing Peter to pay Paul—there is no surplus available as a result of the transaction. How, then, the reader will ask, does it operate, since it obviously is not without result? It operates simply as a tax on subsequent production. The citizens borrow, say, 200

millions, given to them in notes printed for this express purpose, and hand them to the State Bank as subscriptions. The notes then come back upon the citizens, demanding their goods and services. But why bother at all with subscriptions and mortgages? Why not simply issue State notes to whatever amount is required? Yes, but apart from the indebtedness to the Loan Banks contracted for subscribing to the war loan, the citizens cannot absorb more notes than are necessary to carry on the trade exchanges. As soon as there is an obvious excess, the notes would begin to depreciate, and would continue depreciating, until the total exchange value of the notes in circulation corresponded to the total of exchanges which they were required to effect. Now, however, the citizens require an additional 200 millions of notes to redeem their mortgaged property or securities, and they can only get these by producing surplus wealth to that value of the kind required for the use of the State. When that mortgage debt is paid off, the process is ready to be begun over again. The nominal amount of any one loan therefore depends upon the total national assets, and the extent to which the owners can be induced to mortgage their possessions. If, for instance, the total wealth of Germany can be put at 15,000 millions—a modest estimate—and the safety margin at as much as one-third, then the citizens could borrow a sum of 10,000 millions, and notes could be issued to that amount. Whether the people could redeem such a sum, or anything like it, in the course of the war—in economic reality, whether that portion of the nation employed in productive work could create that much of surplus wealth in that time—is quite another story. If they could not, then the note issue would be inflated, and proportionately depreciated, so that the larger quantity of notes would exchange for no more goods than that for which a much

smaller quantity exchanged before the inflation; and the real loan—*i.e.*, the maintenance store—would be less than its anticipated quantity by the amount of the depreciation. If, after the war, the State wanted to restore the notes to their face value compared with the coins which they are supposed to represent, it would have to provide gold for their redemption, at any rate at their depreciated value, and then start afresh with a convertible note issue. Whatever of the mortgages remained unredeemed would constitute a crushing burden on the citizens for many years to come.

Thus much for the inherent nature and possibilities of the scheme of loans by notes issued against mortgaged property. Of course, such a scheme need not necessarily be carried to excess; and provided the amounts which the citizens are induced or forced to subscribe by borrowing is such that they can redeem out of current income by the aid of frugal living, no harm is done by the method. On the other hand, it has the decided advantage of being a much more effective instrument for compelling economy than subscriptions out of savings, more often than not made without incurring the necessity of curtailing any customary habits and indulgences. At present, there is no doubt that we have not yet discovered the right means of enforcing economy and saving—a matter by no means easy to manage apart from the direct way of taxation. As yet there are no clear indications that Germany has carried her method to excess. Certainly the exchanges are heavily against her, and prices have risen enormously; but this can almost wholly be accounted for on obvious grounds other than a serious inflation of note issue. The system of subscribing out of savings has, however, the advantage of a natural channel, as it were, for draining the surplus wealth which the nation is spontaneously

producing, without the least danger of deranging the currency or of undue strain on the economic structure. Finally, whatever the machinery, a war can only be carried on by means of (1) accumulated stock, including gold (which, however, is as far as possible kept back as a reserve); (2) by selling abroad (in effect exchanging for goods) securities representing foreign investments; (3) by borrowing abroad; (4) and, lastly and mainly, by the consumable wealth created from day to day by the nation. We think and speak of saving in terms of money, but behind that is the reality of a surplus of consumable wealth put at the disposal of the State.

In our brief analysis of war finance we have incidentally covered much of the ground we should have had to traverse in reaching the main issue towards which our currency inquiry has been converging. The question of note issue has always given rise to much diversity of view, some well-reasoned, some crude, and some fantastic to a degree. The Bank Act of 1844, which gave the Bank of England a practical monopoly of note issue, has always been much contested. In the first place, there does not seem to be sufficient reason for the monopoly. This, however, has become of small consequence with the present development of the use of the cheque; and I doubt much if the banks are hankering for the privilege, at any rate on the present terms. Then, the limitation of the issue to a gold reserve (apart from the inelastic quantity of securities already mentioned) is seriously in question. In one very important respect, the policy adopted by bankers has considerably altered since the middle of last century. At times of industrial crisis—which, as we know, occurred roughly at intervals of ten years—with the consequent stringency of commercial credit, it used to be the policy of

bankers to restrict the loans given to their customers, and to call in much of the credit out on loan. This was the natural consequence of their fears of a run on their available cash, on the principle that the larger the amount lent the greater would be the risk of a demand for gold. But gradually experience has demonstrated that the supposed remedy was often the very cause which precipitated the catastrophe it was intended to avert. The restriction of bank credit superimposed on restriction of general commercial credit resulted in such distress that it brought on panic and bankruptcy which might have been avoided by more liberal credit. The consensus of opinion is now the other way about—that in time of commercial depression the danger is best warded off by a policy of more liberal advances—though in practice, this policy is by no means carried out consistently by all the recognised banks. The argument against the rigid limitation of the note issue is, that the inelasticity prevents a necessary increase of currency just at those times when, owing to restriction of commercial credit, there is room for extra currency to fill the depleted channel, without danger of excess under sensible management; while, on the other hand, in times of normal prosperity, the bank can well be left to use its judgment, based on experience, as to the amount of reserve necessary to ensure against the demand for conversion into gold, just as banks are left to decide what reserve is sufficient against deposits; and that the mere fact of the note's convertibility is in itself sufficient security against inflation. It is freely contended that much of the distress arising in times of trade depression is distinctly due to the inelasticity of the note issue and to the general restriction of bank credit.

This brings us to the central question, whether the issue of legal-tender notes should not be wholly in the hands of

the State, backed by the security of the nation. There is very much indeed to be urged in favour of such a course, and apparently very little to be urged against it. Whether issued by banks or by the State, the notes in circulation constitute a tax on the community to their full exchange value. The fact that a gold reserve is kept does not alter the case in the least, except that the proceeds of the tax goes, to that extent, into the hands of the gold-producers. There is, however, this all-important difference between private and State issue of notes; that whereas in the former the nation is taxed in favour of a few individuals, in the latter the tax is paid to the Government. The paper currency could emanate direct from the Treasury. It would then be issued in payment of salaries, wages, and accounts for all kinds of supplies in connection with the Army, Navy, and Civil Services. The citizens would then redeem these notes, by giving up in exchange the results of their labour for consumption by those who are in the service of the State—just what all taxes in effect consist of, though paid in money or bank credits. But as the maintenance of the State services must in any case be a tax on the citizens, whether levied this way or that, the citizens are clearly the gainers, since they pay nothing for the use of the currency beyond the bare cost of management. To whatever extent the Government finds it expedient to keep a gold reserve, the tax is paid to the gold-producers; but if, as is demonstrated by experience, notes backed by the nation as a whole require less gold reserve than a private issue, then to that extent it would be a further gain to the nation. Or the notes could be issued through a State Bank, with the same result. With no arbitrary limit placed on the issue, and with the confidence inspired by the national guarantee, in times of crisis the issue could be expanded without risk to whatever extent it may be found necessary, thus

materially easing the strain, while the main causes of the depression are being gradually modified and finally removed.

The question whether a note issue guaranteed by the State needs to be convertible on demand is, when all the obvious limitations are kept in view, more of an academic speculation than of practical importance of any consequence, so far as this country is concerned (at any rate in normal times). We employ an enormous amount of currency, running into many hundreds of millions, but the great bulk of it consists of cheques and mercantile bills. Unlike a note issue, which taxes its users to the full exchange value, the mercantile world pays for this currency no more than a small commission to the manipulating Bankers and Accepting Houses—in effect, a renumeration for administration and management. It would be both stupid and useless to attempt to displace this currency by legal-tender notes. The mercantile community is not going to submit to be taxed an additional 95 per cent, or more, after having in the course of centuries elaborated successfully so wonderful a system of cheap currency. Obviously, the problem rather is how to cheapen the currency still further—how to make cheques, bills, and other personal promises, made current by banking credit, function as the tool of exchange, in place of gold or notes. Our normal note circulation fluctuates round about 30 millions, rather less than more. The question of convertibility involves, therefore, a matter of something under 20 millions—certainly not a formidable sum for a gold-standard country like ours.

But beyond the question of note issue, there is still the wider and more important question whether the State should not undertake the business of banking. It has long been freely contended that our present banking system

fails in some very important respects, to some of which allusion has already been made; and the war has certainly thrown a fierce light on that failure. We are all asking ourselves: If the security of the nation has to be called in to save the banks from tottering to ruin in times of crises, why should not the same security be employed by the nation to its collective advantage? Many of those who have hitherto given little or no thought to the subject have become aware that the German banking system is superior to ours in some very important respects, and that it has in no small measure been the cause of Germany's economic prosperity during the last sixty years. The failure of our banking system to serve the nation's economic needs may be summarised as follows:

(i) It is far too centralised, to the detriment of local industry, particularly that of agriculture. In the old days of small private banks, the manager of each bank was in close touch with the pulse of the local industry and requirements. It was his business to know the status of the local farmers, traders, and manufacturers, and to assist them with the bank's credit. The savings effected in the locality went to foster local industry. But during the last thirty years or so, a change of enormous magnitude has taken place in our banking system. Like Aaron's rod, the big banks have swallowed the little ones, and the biggest have devoured the big; and now the business is in the hands of a few powerful corporations, centralised in London, acting practically in close combination, and completely dominating the financial life of the nation. The local branch is little more than an annexe of the central office, the manager knows little of the local life and needs, and is perhaps as little interested; the security demanded is such that the local farmers and traders are not often in a position to give, and the business of the branch is, in the main, merely to serve

as feeder to the central establishment, from where it is controlled. This perhaps a little overstates the case, but it gives correctly the principal trend. At any rate, the complaints have long been loud and heavy, and it has been recognised on all hands that agriculture has been badly handicapped for want of banking facilities.

(2) London Banking has become of international character and importance. It is in the very nature of centralised banking on a huge scale that the security demanded for advances should be of a fluid character, readily realisable in an open market; and that large undertakings and large capitals should be favoured to the detriment of small undertakings and small capitals. Provided high ability went as a matter of course with large capital, this would be a decided economic gain, but it is by no means safe to take that for granted; at any rate, the automatic squeezing out of the small capitalist by an inexorable banking system bent on making profits does not seem quite the right selective process. If there is to be any selection in lending on grounds of ability, let it be done after due investigation on strict merits. There is, of course, another side to this picture. The magnitude of the banking combine, with the system which it necessarily involves, brings into the country a very considerable income from abroad, in payment of banking and discounting facilities. In this London is quite unique—there is no place in the world to approach it in this respect. The problem, therefore, is, Could a State Bank, or some form of State control, leave this income from abroad secure, while at the same time rendering greater facilities to the small capitalist?

(3) Banking on this scale ceases to be national in character and intent. The banker, like every other business man, is out to make profits, consistent with high security for conserving future profits. If, then, he can make better

commissions—and in part himself investing his own or his clients' money in expectation of subsequent "unloading"—in promoting loans from abroad, it is not his business to consider whether the money could have been more usefully invested at home. As it happens, the interest and commissions offered by borrowers abroad have always been considerably higher than that offered for similar flotations at home, and of recent years with very excellent security. In the view of many competent authorities, the result has been that home investments have languished sadly, while British products went out for investment abroad.

But let us be quite clear on this point. Many of my readers will probably have read the complaint that many of these investments are used for building railways, factories, and ships to compete with our own industries; and that this is, *per se*, an unjustifiable hardship upon the industries subjected to this competition—that our wealth should go abroad for building up industries to compete with ours! But this is altogether an uneconomic way of looking at it. No doubt a railway in Argentina, creating transport facilities through a vast farming district, competes seriously with the farmer at home. But if, apart from other causes, the farmer at home cannot hold his own with the Argentine producer, after the latter has paid the higher interest and commission on the loan together with the cost of the long transport, it is time he gave up farming and took to making mouse-traps. I said "apart from other causes." One has just been dealt with, *viz.*, banking facilities; and the other is that the whole of our land system—ownership, rent, restrictions, lack of co-operation in transport and distribution, etc.—wants considerable overhauling. That a vast grain-producing district should be made fruitful, and its products available long distances away, is a great gain to

the world; and particularly so to the country which has a claim on that district for interest, and which, from the extent of its land and industry, must rely for some of its food-supplies from abroad. No, the hardship is when the products invested abroad are also needed to set going, or to back up and extend, a remunerative industry at home. It then becomes a question of setting the gain from establishing or extending a home industry against, perhaps, no greater or even a smaller gain of opening up a desirable industry somewhere abroad; not unmixed with the natural sentiment that when it comes to weighing one against the other, the home industry should have the preference. A State bank would, and should, give home investment the prior claim, even though at a less interest.

(4) Under our present system, the inventor and man of ideas, without capital, has very little chance indeed. If he is energetic or lucky enough to interest some of the promoting fraternity, much will depend on whether his idea can be made attractive enough on paper to draw the public, and nothing will be done unless the promoters can see their way to appropriating a large slice of the money subscribed. It is nobody's business to see that an invention which promises good results shall have a fair chance. The history of the discovery of the chemical dye process is a classic instance in point. The German method of handling ideas and inventions has been for many years the very opposite to ours. It is the business of the State Bank, as of the other banks, to assist and foster trade in every possible way, to investigate carefully all ideas, inventions, and business propositions submitted to them, and if they promise good results, to give them a fair trial. The State employs a large number of scientific experts—*e.g.*, analytical chemists, whose duty it is to discover new processes and compounds. Many a British idea or invention which

no one at home could be induced to take up has found its way into Germany, and has proved successful. In short, the banks are designed to co-operate with the State, instead of being merely exploiting tradesmen.

(5) Lastly, there is the point already dealt with, that in time of crisis the restriction of banking credit is still far more stringent than it should be; and that only a State Bank, with the security of the nation behind it, is in a position to remedy this evil to the full extent which the circumstances demand, without fear of a monetary panic or breakdown.

Such are the arguments for a State Bank; and, in the main, I can see no effective way of rebutting them. It is beyond question that our banking system would have utterly collapsed in those terrible days of August, 1914, with consequences too appalling to contemplate, had not Mr. Lloyd George and his advisers come to the rescue, backed by the patriotic goodwill of the nation and the press. The German nation is accustomed to be dragooned and to obey orders; but that the British people should have settled down readily to Moratorium and Treasury Notes, accustomed as they were to handle gold at pleasure, is vastly to their credit. The banking business is far too important to the life of the nation, and far too exclusive a monopoly under present conditions, to be given up to private exploitation by what is in effect a closed-up ring. If the State is to come to the rescue in time of trouble, there is certainly no reason why it should not share in the income in times of prosperity.

The matter is, however, not without much difficulty and complexity. The complicated machinery of lending and bill-discounting cannot very well be under direct State management and control. Place the limit of State action where you will, it is tolerably certain that the management

of private loans—the discriminating between the multitude of applicants, the weighing and balancing of their business standing and credibility—is the very last thing in the world that should be undertaken by a State Department. Even during the short period when the Government guaranteed the Bank of England against losses in discounting *approved* pre-war bills, there was a debate in Parliament about a refusal to discount the bills of a certain firm, suggesting bias or prejudice on the part of a member of the Government. One can well imagine the tremendous outcry and charges of favouritism, corruption, and what not which would constantly be launched against Ministers and State officials entrusted with the administration of such a department. The way to escape this is to place that part of the business under the independent control of a Board of Management, giving them an entirely free hand, but with general instructions to give a ready hearing to new ideas, inventions, and business propositions, and to investigate the apparently promising ones with the aid of scientific experts appointed for the purpose. If no agricultural banks are established expressly for aiding the farming and local industries, the State Bank should open branches all over the country, with express instructions to foster the local farming and industries. With the backing of the nation behind it, an occasional loss could be borne with equanimity, in the knowledge that, on the whole, the national gain was greater than the loss, even if it did not always show as an actual profit. The note issue, convertible on demand, but freed from the condition of a fixed gold-backing, could be under the direct control of the State, capable of expansion in time of crisis. The condition of convertibility, coupled with vigilant care, such as bankers know how to gauge, would be sufficient to guard against inflation.

In conclusion—serving by way of a much condensed summary—I think it necessary, now that we are in a position to take something like a comprehensive grasp of the problem, to say my final word round the question of bank credits, which has already been dealt with with some care. More than once we had to remind ourselves that the science of Economics is unfortunately burdened with a "market" terminology of much ambiguity. But I doubt if in the whole range of the English language there is anything to approach the strange freak which has made the term "credit" a constant shuttlecock between two diametrically opposed meanings, not unfrequently used in the same sentence or phrase, to the utter confusion of thought and valid reasoning. Indeed, I have a strong suspicion that I am by no means free from guilt myself—the term comes so readily to tongue and pen by sheer force of habit.

You give John Brown a credit entry in your ledger when he has paid what he owes you, not when he has contracted the debt. He is then a "debtor," and it is you who hold the credit on him; yet you will say that you have given him "credit." You hold a genuine credit on your bank when you have deposited something with them. A credit, in short, is a claim on someone for something lent him, or sold to him (a distinction in word only), on a promise of return or payment later on, and the borrower or buyer "on credit" (should it not be "on debit"?), is, of course, the debtor. Yet in the same breath you will say that you can get credit at your tradesmen, or in the market generally, for so much. But what you will get will be a "debit" or debt—it is the lender who will get the credit. What you really mean is, that your reputation is good enough to make people lend you—you use the word debit in the sense of "credibility" or trustworthiness, meaning that people are ready to trust you. You cannot have it both

ways—you cannot hold a credit when you have lent and also when you have borrowed! In the same way, one speaks of national credit collectively; but what one really means is the readiness of lenders to trust the nation's ability and intention to pay any debts it may contract. A nation holds credits on the United States, for example, when it has issued loans to that country; but when it borrows from it—what you are pleased to call getting credit—it is the United States that will get (or hold) the credit: the borrowing country will have the debt, or debit. The careless use of the term would, however, matter little, but for the fact of some huge and grotesque blunders which have been, and are now being, built up on this double meaning. Conclusions more or less valid are arrived at as to the actual or possible function of true credit, and the conclusion is then bodily transferred to the spurious use of the term, manifestly with disastrous consequences.

A brief summary of the producing mechanism operating by means of currency—the vehicle which carries and distributes, as it were, the life-preserving utilities throughout the economic organism—should now suffice to clarify the position to crystal clearness. Man begins by being his own universal provider, and is miserably poor as a consequence. Presently one who had been hunting in the morning and intended to go fishing in the afternoon, meets on his return home another who had employed his morning in fishing. Both have had good catches, and the thought strikes them that they might barter. After several such experiences, the conviction gradually forces itself upon them that they could both do better by each sticking to one principal occupation, and bartering the proceeds. Other occupations get similarly specialised, and so we get the beginnings of the economic organism—the specialisation of functions, with some co-ordination of several functions to a common end.

But with each specialisation the process of barter becomes more difficult. Middlemen become necessary to do the carrying and distributing. Before this stage is actually arrived at, it had probably been found that the thing had already become too complicated for simple, direct barter. We can pass over the intermediate devices, contrivances, and stratagems, and come to something which would correspond to modern paper currency. The hunter gives up his product to the middleman, and gets a receipt from him in terms of some recognised unit. The middleman, being well known and trusted, his receipt, or IOU, runs current among the local shopkeepers. The hunter goes to a shop and changes the receipt for flour, eggs, butter, and cheese. With the aid of the piece of paper, he has bartered—we now call it "exchanged"—his products for these commodities. The middlemen and shopkeepers correspond to what we have agreed to know as "the stream of production," into which a vast multitude of conduits, rills, and rivulets are constantly discharging products. Our hunter contributes to one part of the stream, and draws out an equivalent from another part. The shopkeeper then gets his equivalent (the reward for his services is included in the added price on the goods supplied to the hunter) when the middleman brings him his stock of flour, etc. from the farmers, with which the receipt is redeemed and destroyed, and the exchange of things is completed.

But presently a super-middleman steps into the arena. The middlemen, A to Z, are of all sorts, some rich, some comfortably off, and some just struggling along. The shopkeepers are spread about, the goods travel over longer distances. One shopkeeper who knows and will trust A, knows nothing of B, and another who knows B, knows nothing of A or C. Some are trusted for a great deal, others for less, and some for very little. Then the banker

steps out before the crowd, tells them that their old method is breaking down under the stress of changed conditions, and says that he has a much better, safer, and more sure way. What is this way? they all want to know. Then he explains his scheme.

"I want to be your banker. To begin with, all of you should deposit with me whatever claims you hold on the stream of production, by virtue of having contributed goods or services thereto, whether these claims are in the form of gold, silver, receipts for goods from your buyers, or some other instruments which form valid credits on the 'stream.' You must look upon this as part of your stock-in-trade. When you buy goods, instead of giving the seller a receipt or IOU, which may or may not be accepted by the shopkeepers of whom he wants to make purchases, give him a demand on me as your banker. The demand will be in terms of so much gold; but as he will not want gold—nobody really wants gold except for some special reason—he will take my promise, which will run current in payment of purchases, without question or demur. When you have sold the goods and received also a bank credit for it—as you will when once the system is established—pay that in to me, and that will make good the debit entered against you when you gave the claim on me on purchasing the goods. You know that my reputation is good, and that everyone within a large radius will accept my paper, and I will appoint agents wherever necessary to see that there is no hitch. This is my scheme for a safe and cheap currency working smoothly and evenly, which I don't think can be beaten."

"Very plausible indeed," replied the listeners in chorus. "But where do you come in? What is your object?"

"Well," replied the banker, "candidly I am not a philanthropist, but a business man like yourselves, and I will

tell you where I propose to come in. There will always be a balance of your deposits in my bank—if you let an account run down too low, there will be a banking charge. Now, you know the principle on which certain Building Societies, or working-men's Loan Clubs, are run. A number of members pay in weekly or monthly premiums, forming each week or month lump sums, which one of the members can draw as a loan, by lot or rotation, on which he pays interest. I propose to work my bank something on this principle, except that, unlike the Building Society, which is terminable, mine will be interminable. Your business requirements don't run evenly from week to week and from month to month. Sometimes your stock capital is more than ample, at others there is a pull on it, and sometimes the strain is rather severe. At certain seasons you have to buy more largely, and all sorts of untoward events and combinations take place. In times of strain, then, I should be ready to lend you money, perhaps I should say bank credits, at a very moderate interest indeed. Of course, you would be borrowing your own—that is, your own collectively, not individually, or you would not need to borrow. But this is the principle on which all Associations are founded. It is the principle on which all social life, all economic life, all financial life, has its being—to use the collective funds and resources to ease the strain wherever it may be, first here, then there. You are all creating wealth, and a surplus remains for the time in the 'stream,' to be demanded by whoever gets the claim on it. I will be the custodian of these many claims, collected, as it were, into one large central pool; and I will lend those claims—of course, on sufficient security for repayment—to ease the strain wherever it may happen to be, just when it is wanted, first to one, and then to another of you, and so prevent any obstruction or stoppage. You will not be all wanting it at the

same time, and naturally you will not pay interest needlessly. That interest will be my reward for organisation and administration of your funds. It will be mutually advantageous, and will add to the wealth of the world."

Bank credits having taken the place of metal currency to all but an insignificant extent, it obviously becomes a question how to utilise the bank credits to the best advantage, and to their fullest capacity. No undertaking or enterprise, actual or proposed, should be crippled or stunted, so long as there is bank credit available to be lent, of course on undeniable security. If, for example, the banks in this country are the custodians of claims on production to the amount of 1,000 millions, it is a question how much of that can be lent without risk to the banks' stability; and there is clearly legitimate ground for differences of opinion as to that, as to the nature of the security that should be demanded, what interest ought to be charged, and other details. The claims of which the banks are the custodians represent wealth contributed to the "stream," which can be used for thousands of different purposes. They can be used by idlers on freak luxuries, by the vicious in promoting vice. If, instead of drawing food and clothing to feed and clothe a pet monkey and its twelve liveried servants, it were drawn to feed and clothe a number of men engaged in experimenting on some attempted chemical discovery, or new method of organisation, even if that fails, and the labour is equally wasted, it is surely less of a loss than breeding a contemptible race of soulless menials, without initiative or enterprise. On the other hand, the gain from one successful discovery may prove far greater than the loss from a thousand failures. If a portion of the bank credits acting as currency are in the form of legal-tender notes—to which, of course, the State must be a party—

other questions arise, to which we have already given as much space and consideration as our limited scope demands and permits.

But here comes the confused thinker and would-be "Currency Reformer," whose arguments and conclusions, if not water-tight at every point, are, at any rate, within the legitimate field of discussion as applied to true credits, who straightway transfers his conclusions to the use of the term in the diametrically opposed sense. His reader or listener, who habitually uses the term in the same double-faced way himself, fails, of course, to detect the leakage. The Economist, Banker, or Financier knows as a fact of history that it is all wrong—it has been tried and failed dismally—the very financial atmosphere of his daily experience makes him feel that the thing is preposterous, yet he cannot put his finger on the flaw. The hard-pushed business man, the man in the street, seeing a vista of money galore, rejoices exceedingly, and prepares for the millennium.

If bank credit is good money, why not extend bank credit? Why should anyone go short of money so long as he can give sufficient security? Had money meant gold alone, there is, of course, only a limited quantity of it; but since it now means bank credit, why not *make* bank credit to whatever extent is demanded? If the banks will not do it, then the State must take it up: it must be made compulsory to lend bank or State credit on sound security. One "Reformer" would have the banks or State lend entirely free of interest! Why should industry be crippled wantonly, and thus heaps of wealth lost to the nation? The thing is simple enough. A man in business, or wanting to go into business or enterprise of any sort, is short of money, but he has good security—fixed property, as land, houses, factories, and shops; movable property, as furni-

ture, pictures, jewellery, etc.; machinery and trade plant, and also trade stock. He can mortgage or pledge these to the bank to their market value less some safety margin—say one third, or even so much as one half, if you like—and get in return a credit entry in the bank's books, on which he can draw by cheque. If the "Reformer" knows something of banking business, he should know that machinery and trade plant, and even factory buildings, are the most hazardous security possible. Many a bank has come to dire grief by advancing on this class of security, but this is only a detail.

Our banking figures on page 132 show that out of deposits of 1,000 millions the banks had out on loan some 735 millions, roughly three-quarters of their deposits. At present the banks lend very little on the security of property, fixed or movable, the bulk of their securities for loans consisting of fluid paper. The capital wealth of this country is variously estimated anywhere from 16,000 to 26,000 millions. Put it at what you will in reason, it is clear that this scheme of creating new currency on the security of the nation's assets would threaten to flood the country with anywhere from five thousand to ten thousand millions of new currency! At this our "Currency Reformer" is not in the least dismayed. "Why not, so long as the security is good?" But what if the banks, lending far beyond the amount of their deposits, are called upon to pay in gold? "Oh, make it inconvertible legal-tender paper—the nation's credit is good enough." It would be idle to argue with one so far gone in "mental vertigo."

The root fallacy is to be found in the use of the term credit for what is really a debit. First, take the case of a depositor's cheque. You pay Smith by a cheque on your bank; the credit on the bank forms the currency. But what is behind that? Why, your credit on the bank

represents something you have given up for others to consume, and when you transfer that credit to Smith, you get the equivalent which completes the exchange. Possibly, your personal IOU could have served the currency function; but the intermediation of the bank makes the process much more certain, expeditious, and safe. Next, what happens if the bank lends some of the credit which you have deposited with them? Why, it only lengthens out the process of the exchanges. Thus, the credit with which you might have got the equivalent from Smith is handed to Jones, who gets something with it from Brown. But Jones uses that something for producing more wealth. Some of this he sells to Robinson, receives a bank credit in payment, and with that liquidates his loan at the bank. That goes to make good your deposit, and is ready for you to get something from Robinson, instead of from Smith. What actually makes the currency is the fact of the credit—the fact, that is, that something has been given up. The intermediation of the bank is merely an incident in the process, made necessary by causes mainly psychological in their nature. As we have frequently repeated, anything can be currency, when it is indispensable as a tool; but when it does not consist of true credit, it has to be paid for to its full exchange value, and there is no inherent check against inflation. Whereas the currency of *bona-fide* credit is the true equilibration of exchanges, is entirely free from the risk of inflation, and costs no more than a commission, or charge for management. It has been slowly evolved through centuries, but there is still room for much improvement.

By all means, let the banks make the utmost practicable use of their deposits, in support of the trade of the country. If at any time there is an obvious shortage of currency, and it becomes necessary to create an issue guaranteed by the

State, or by a national bank, let it be done deliberately, with all due precautions against inflation. But for banks to go on lending beyond their available funds—a currency of "debts," not of credits—letting loose an avalanche of currency, running into thousands of millions, based on the assets of the nation, is the straight road to economic perdition and red ruin.

P.S.—Since this chapter has been rewritten, some of the figures have been considerably augmented. But as they do not affect the argument, it will be sufficient to mention the fact.

Events are more than amply confirming what is said in the last chapter that there has been a deplorable amount of wasted effort in our midst. The war is proving incontestably that there is a large store of reserve energy which is not being productively utilised in normal times. If that were not so, our economic stability would long since have collapsed.

Last, but by no means least, it is proving triumphantly the enormous power and efficiency of organisation and co-ordination. We see it so plainly on all sides that there is no need to elaborate it. May the impression which it is now making prove deep and lasting.—*April, 1916.*

CHAPTER XVI

SOURCES OF WEALTH—NATURE AND THE HUMAN FACTOR—COSMOPOLITANISM AND NATIONALISM—FREE TRADE *v.* PROTECTION—COMPARATIVE COST—INTERNATIONAL TRADING: WHAT GOVERNS THE RATE OF EXCHANGE

THE primary fountains of national wealth are the resources of its soil, climatic conditions, geographical position in relation to other countries, and the extent of its seaboard and harbours, fitted by nature for safe and convenient anchorage. One country has rich agricultural soil, another has gold deposits, another has an abundance of iron or other metals, another has deposits of mineral oil, and another—*e.g.*, our own—has large coalfields. The particular products which the soil is capable of yielding depends largely upon climate. We depend for our tea and many other things upon Eastern countries, for cotton upon certain American States; and so on through a long list that may be compiled of the chief products of various countries. By each developing its own resources, and exchanging with the rest, the world, as a whole, is more amply provided with the things requisite to sustain life in comfort, and to satisfy the many human desires.

To picture, however, that the contrast between the wealth of various countries is wholly the outcome of their several resources of soil, climate, position, and harbourage, would be a most stupendous blunder. Many a country and

district of high fertility and rich mineral deposits remains poor as a result of the sloth of the inhabitants. On the other hand, we have the striking example of Holland, where a country much of which might for ever have remained a useless swamp, has been turned into fertile land and navigable sea, capable of providing comfort for a large population, by the industry and ingenuity of its inhabitants. Granted, of course, that the natural resources must form the primary fount of a nation's wealth, it is impossible to say how much of it is the result of soil and climate, and how much the result of the human factor, or where the one leaves off and the other begins. Except only the world's deserts, such as the Sahara—and even that could be turned into a great lake capable of navigation—or the extreme arctic regions, there is not a soil in the world that cannot be made richer and more life-sustaining by the industry and inventiveness of man. Even in such relatively simple matters as the agricultural fertility of soil, it is difficult to draw the line between natural and man-made (not meant as a contrast to "natural" fertility). Irish cotters have made many an acre fertile by covering their holdings with a coating of soil carried from some considerable distance in basketfuls. Ground is cleared of stones and scrub, swampy ground is drained and reclaimed, the land is manured, districts are made accessible by networks of railways and canals: all made fruitful by the hand and brain of man. When we come to the industries in which vastly more depends upon human service, ingenuity and inventiveness before the natural raw materials can be made subservient to man's needs, the human factor stands out pre-eminent. In short, with the natural resources of a country must be intimately coupled the stamina and genius of its people, industrial habits which it may have acquired in the course of its development,

and last, but by no means least, the education and training, physical, intellectual, and moral, which fit it to engage in the struggle with nature, and—to the shame of the human race, be it said—in the struggle with its fellows of other nations. Nevertheless, it would be a serious mistake not to realise that one or two strikingly outstanding natural advantages may often make a vast difference between success and failure. Without doubt, the abundance of cheap coal, coinciding with production by machinery, and coupled with facility of transport by sea, has been the main cause of our prosperity. Starting with that important initial advantage, other advantages inevitably followed; and the very habits of industry and initiative grew as a result of the powerful impetus imparted and sustained by the natural gift. Success is a great tonic and fertiliser.

We have had occasion in our last chapter to refer to the school of thought which conceives every economic advance by a foreign nation as so much ground cut away from under the feet of our own nation—so much potential trading and profit-making fallen into the hands of others which might have been ours instead. We cannot prevent other nations looking after their own interests, and it would be idle and ungracious to complain; but when our own surplus wealth is sent abroad in order to enable foreign nations to develop their resources—to build railways, canals, tramways, mining machinery and plant, electric power stations, factories, and what not—these good people complain bitterly that our own wealth is made into rods to scourge our backs—that a host of competitors is being raised to compete with our farmers, miners, manufacturers, and traders. There is, on the other hand, the very opposite school, grown up, perhaps, in keen protest against the Mercantile Theory of Wealth, and is generally known as the Manchester School, which

maintains that every advance by every nation the whole world over—every potential resource of soil, climate, harbourage, and national initiative and energy developed and made operative—is so much added to the world's total wealth, which benefits everybody. What you call trading is nothing but exchanging; what you call profit making is nothing more than obtaining by way of exchange, in addition to the cost of the material, an equivalent for the services rendered by the trader or middleman, be he manufacturer, merchant, entrepreneur, or financier. The more a nation produces, the more it will be ready to give of its products in exchange for the products of other nations; and the more all the nations produce between them, the more there is to go round. It is the most stupendous folly to suppose that when a foreign nation has developed the power of producing more wealth than it was previously capable of doing, any other nation can possibly be the worse for it. They may increase their consumption to the full extent of their increased production; but as the additional wealth is probably confined to some few things, which remain as surplus product, they will want to exchange that with other nations, who will get the advantage of an increase in the terms of the exchange, as an inevitable consequence of the increased supply. At any rate, it is impossible to get away from the hard and solid fact that more wealth is being created; and that being so, there is no escaping the conclusion that there is more to go round. And so we get what may be termed the International or Cosmopolitan School, which conceives every economic advance by every nation, whether it be in the field of extracting, manufacturing, or trading, to be an advantage to ourselves, without any sort of qualification.

We shall find, however, that this view of the matter cannot be stated without qualification. That the development

of the potential wealth of any country—vast agricultural districts, mines yielding metals and minerals of various kinds, tea, rubber, and cotton plantations, and a thousand and one other sources of new wealth—can possibly be of injury to any nation, in the long run, is, on the face of it, preposterous. That every new development puts at a disadvantage for the time being someone who is already engaged in that or some kindred industry is, unfortunately, only too familiar in our midst at home. The man who opens a more efficiently organised shop across the road takes away some of the trade of his neighbour opposite. The factory which sets up to turn out articles already on the market, particularly with more modern machinery and methods, lowers the price of the commodity, and puts out of joint the business of those already engaged in it. That the discovery of some new preparation, new machine, new contrivance, destroys the demand for the old preparation, old machine, or old contrivance, and throws many workers out of employment, is a familiar phenomenon. So familiar is it, and so much have the bearings of the subject been discussed, that it would be a sheer waste of time to elaborate the argument here. Everyone with a fair share of robust sense must see that to shut off new machines, new discoveries, new preparations, new and more efficient methods of organisation, because such changes injure others already engaged in enterprises which the new methods will displace, would obviously be suicidal. The nation which hung back would simply be outstripped by more enterprising nations, and left stranded high and dry. That workers trained to an occupation cannot easily adapt themselves to new machines and methods is an inevitable natural deficiency, against which nations should provide by some scheme of insurance, or State help, until the new generation is trained to the new machines and

methods. Economy in production means increased product for the same effort (p. 83). The nation is the richer for every new machine or method which, in the language of commerce, economises cost. I think most of us can see that clearly enough as regards home industry; but a good many seem to be unable to reconcile themselves to the thought in regard to foreign industry. They somehow fail to see that the more another nation produces, the more it has to exchange for our products—as we should say there is an increased demand for our goods—and that the more it economises in its cost of production, the more favourable the terms upon which it is prepared to exchange with us. If, for example, 100 units of a particular product are produced at the cost of 100 units of labour, they will, *ceteris paribus*, exchange for so much of our product as also costs us 100 units of labour. If that nation, by effecting economy, is now able to produce the same 100 units of product for 80 units of labour, it will, in the long run, be prepared to give us that 100 units of product in exchange for that much of our product as only cost us 80 units of labour to produce, instead of, as heretofore, demanding that much as cost us 100 units of labour to produce. It is not a question of goodwill, but simply of supply in relation to demand.

But this does not present the whole case—there is another facet, perhaps several facets, to the crystal. We have hitherto used the term "production" to mean all useful services whatsoever, and the definition has served us admirably. But now, for the purpose in hand, we must draw a sharp distinction between extractive industries on the one hand, and manufacturing and trading on the other hand. Apart from actual physical war, a nation cannot be hindered by other nations from increasing its income and accumulating wealth by developing its resources of

soil, climate, and physical and mental capacity—*e.g.*, by opening up new mines, draining and reclaiming land, afforestation, acclimatising new agricultural products, and by other ways as means to ends, such as more effective organisation and co-ordination, better education and physical training. If other nations also develop their possible resources, there would be an all-round gain; for though the increased supply of the products of one nation would necessitate its giving more by way of exchange to other nations, whenever such exchange was desirable, their increased supply would mean a corresponding increase to her. In a word, there would be more of things in the world available for consumption. Not unfrequently it may be a question which of two or more possible developments is likely to prove more advantageous. Thus, it may be a question whether it would be best to use the available labour and capital for reclaiming some swamp or foreshore, or for opening up some new mine; for though the food which could be grown on the reclaimed land is the actual necessity, yet it may well be that the metal extracted from the mine could be exchanged for more food from abroad than could be grown on the reclaimed land—particularly, perhaps, when the time required for the respective development of either enters into consideration.

But besides getting things in exchange for extractive products, nations also get things from others in exchange for services—services, that is, rendered in converting extracted raw materials, whether produced at home or imported from elsewhere, into consumable commodities. In our own case, the great bulk of the things we get from abroad come to us in exchange for services of many and various kinds: manufacturing, carrying by sea, banking and manipulating the world's paper currency, and even by being a convenient centre for finished goods, which, coming

here from abroad, are then distributed to various countries. We export practically no food at all. We do export a great deal of coal, and some products of other mines; but in the latter, the raw material forms but a very small part of the value of the manufactured consignment. Some countries may be getting the bulk, or even the whole, of that which we send to them in return for food, wool and vegetable fibre for making into clothing, hides for turning into footwear etc., and other raw materials—all primary extractive products of their soils, which, in the nature of the case, other nations are bound to want, and to be willing to give an equivalent in exchange, whether in other kinds of extractive products, or in services. But we get the bulk of what we obtain from other nations in return for services rendered.

Here, then, we come to the point—and a point of enormous consequence it is to us, perhaps of more unique consequence to us than to any other nation in the world—where the International or Cosmopolitan conception of economic adjustment must be qualified; or, at any rate, correctly interpreted. Our coal, minerals, and whatever else we extract from our own soil—increased by the invention of machinery and tools, efficient organisation, and the right kind of education—will be in demand whatever other nations may do, unless, of course, new coalfields, etc., are discovered and developed—which is another story. We possess in these what we know as “exclusive access to superior fertility.” But there is no “exclusive access” in rendering service to others unless by our own energy and ingenuity we make it “exclusive”—in other words, unless we can render the services which we want to barter for things abroad better than other nations can do it. But in what way, it will be asked, does that militate against the Cosmopolitan conception of economic adjust-

ment? Certainly, by all means let each nation obtain from others that which it desires in exchange for just those services which it can render better and more efficiently than other nations can. Thus will the prosperity of the nation and the prosperity of the world be promoted at the same time. If each nation produces what it is best fitted for—that which it can make better in quality or greater in quantity, or both, than others are capable of doing—there will obviously be more income, more wealth for everybody. Would you have it so adjusted that the less capable nation should be artificially bolstered up at the expense of its more capable neighbours? And how better can the proper level of merit be found than by open competition? By putting them all on their mettle, each will be doing its best to excel, and themselves and the world will be the richer for it.

All this may be granted most readily. But the chief and primary qualification is, that the business of making the national services of “exclusive access,” so that they are in demand in other countries, must be made a national concern, not left wholly to individual effort. Within the nation itself, we leave economic efficiency to find its true level by individual competition, except for some purely restrictive measures, designed to prevent the strong preying unduly on the weak. Some say that we leave too much to individual effort and competition—that there are many undertakings which, from their monopolistic nature, could, and should, be better and more profitably carried on by the State. Others maintain that, under present conditions, competition is not the best means of developing individual capacity in production, or that, if there is a tendency in that direction in some cases, it is more than counterbalanced by the gigantic social evils which competition brings with it, and by stifling and stunting capacity

in a vastly greater number of cases, for want of opportunity and the physical and moral surroundings and atmosphere which foster capacity and initiative. They, therefore, hold that the nation should collectively own the means of, and carry on, production to the advantage of the nation as a whole, and of every individual within it. As to these views, we shall have something to say in our next, and final, chapter. The intellectual Socialist carries his ideal further than this—to a time when all the nations will be federated in one great and high social and economic aim—to get the most out of nature while making the best out of life, to encourage and give the best opportunities and help to every individual to develop to the utmost whatever he is capable of. We can all pay homage to high ideals, and do our best not to discourage them. Ideals are the nurseries and mainsprings of human progress. We may never reach them, but the striving on the road towards them is the chief factor in moral evolution which leads to social advance. Ideals are never reached, for the simple reason that they become sublimated as we approach them. The ideal of to-day may be (not necessarily is) something more than the kindred ideal of last generation, and something less than that of the coming generation. But since that ideal of a federation of the world's States in one common interest is, surely, yet a tremendous distance away, we must face the conditions as they are, and as they are likely to be for a very long time yet. At any rate, while competition is in being, it is simply stupid not to recognise that in international trading the nation must be the unit, which, in its executive and administrative capacity, must take an active and organised part in promoting and assisting in the competition for trading with other nations.

Germany's economic success since 1871 is attributed

by some to its policy of protection—the usual easy fallacy of *ex hoc ergo propter hoc*—that if one thing follows another, it must be because the latter is the effect of the former. Her success has been due to three main causes, which are more than sufficient to fully account for it. One is, that for the first time she found the opportunity and the means to develop the vast natural resources of the United Empire on a comprehensive and organised scale. The second is, that she set herself to secure economic success by an education and training of her citizens requisite to the aim in view. And the third is, that, apart from taking an active part in fostering production, as already dealt with, she also made it her business to foster her foreign trade, by a well thought-out consular service, and by other means to that end. When a nation makes "six blades of grass to grow where one grew before," it is more than strange that people should stand agape, and go out of their way to discover the cause of the nation's prosperity in juggling with tariffs! Even if, on its merits, they believe that a protective tariff helps a country, that should be no reason for being stone blind to the obvious and most evident causes staring them in the face. Surely, in face of these great facts, it is not unreasonable to infer that Germany has prospered in spite of her tariffs; and that Great Britain, which neglected many of the elements to success which Germany had so assiduously nursed and fostered, nevertheless prospered to a greater degree because of her Free Trade. While, then, Germany, and perhaps other nations, are nationally taking an active concern in looking after their foreign trade, it behoves us to do no less.

It must be further borne in mind that the matter of securing foreign trade is not wholly a question purely of merit. Not unfrequently there is little to choose in the matter of quality, but is entirely a question of effective

organisation. What is known as "salesmanship" goes a considerable way in securing trade abroad, as it does at home. We are supposed to be lacking in many points which go to secure foreign trade; and our consular service is clearly not so well organised for that purpose as that of Germany. I doubt not, some of the qualities of salesmanship are not always of the self-respecting, manly type, to say nothing of being occasionally bordering on dishonesty, and more often mean and petty. We need not compete in these qualities—in the long run they probably recoil upon the "smart" salesman or nation, but there is no reason why we should not approach the potential buyer in a way intelligible and agreeable to himself, and endeavour to meet his wishes in detail, though we may think them only fads. National habits and idiosyncrasies go for a great deal. In a sense, competition in trading is a war—a war of skill, stratagem, and finesse, even where no harsher terms are applicable. It is a great pity that, in the matter of making our services in demand abroad, it often means baulking other nations from disposing of their services—that one nation's gain should mean, to that extent, another nation's loss. But since we have neither the means nor power of organising and co-ordinating our industries with those of other nations—indeed we have scarcely as yet begun to think even of organising and co-ordinating our own industries at home—there is nothing for it but to make it a national concern to promote trading abroad, doing our best to make our services in demand rather than those of other nations. Competition will then still give merit its rightful position in the long run, and we shall not command success unless we deserve it; but at any rate, we shall not let our chances go by default. The keynote to economic progress should be, educate, educate, educate. As a country with a large population thickly

clustered within a small area, it is particularly important for us to make our services in large demand. But let not the reader unconsciously slide back into his old conception of the economic fabric. It is not that we want other nations to take for their consumption the results of our thought and labour. What we really want is to get as much as we can of their products for our consumption. But since we know that they will not give it to us except in fair exchange, then we must make ourselves fit to render services which shall be acceptable in exchange for that which we want. The export is no more than an index of the expected imports. Since it is no difficult matter to decide what we want in exchange for our exports, but a very difficult matter indeed to decide upon the industries and methods which will secure a demand for our services, it is inevitable that in a study of economics the matter of export should stand out so prominently, while the import is, as it were, taken for granted.

There remains for us to discuss here one more important question—the question of Free Trade *v.* Protection. I have never yet heard the case for Protection stated in terms of utilities—come to that, neither have I ever heard the case for Free Trade stated in these terms. But somehow I have a strong conviction that any attempt to state the case for Protection in terms of utilities would break down ignominiously on all essential points. What I believe to be its popular presentation in money terms has already been given (p. 169). I believe that statement to be the very heart and core of the doctrine, and that the rest of the arguments are so many side issues of little or no relevance to the main issue, plus a quantity of figures supposed to substantiate the main doctrine. If some of my readers should think that it scarcely becomes a judicially-

minded writer on economics to condemn so unsparingly, without qualification, a doctrine now subscribed to by so large a section of the community, I can only asseverate that I do so in all sincerity. I think it is so readily subscribed to simply because the man in the street is positively incapable of seeing the economic structure otherwise than as a money-grinding machine; and that it only wants that in its integrity to make Protection a live issue. As soon as one realises the economic structure in terms of utilities, and tries to state the case for Protection in these terms, he will see it evaporating to nothing before his eyes. I have said that figures are given "supposed" to prove the doctrine. For instance, stacks of figures have been published to show that, estimated in percentages, the progress in the foreign trading of Germany and America has been greater than ours in the last forty years. The reason for Germany's progress has been discussed a few lines back; and, compared with us, America is a land of infinite resources and wealth, and the wonder is, not that she is progressing at a faster percentage, but that, spite of her inexhaustible resources, she should still be, and continue to become, our debtor. Then, the matter of estimating by percentages is, on the face of it, so deceptive in a case like this. For example, starting from, say, 100, an addition of another 100 makes the increase 100 per cent.; but starting from hundreds of millions, an addition of 20 to 50 millions makes the increase no more than a few per cent. Manifestly, a nation doing an export and import trade running into many hundreds of millions cannot hope to increase in geometrical ratio, or even in successive arithmetical ratio.

To begin with, let us dispose briefly of two or three side issues, so that we may more easily discover, if we can, what really constitutes the main issue. The first one on which

a few words must be said is of serious importance enough, but is not really an economic issue at all. It is urged that it is highly desirable to protect, *e.g.*, the industry of agriculture, whatever the economic bearings, so as to develop it to its highest capacity, in order that, in the event of war, we may not be dependent quite so much as we are now on imported food. With the aid of our colonies, who are to have a preference—not a free market—we may then be quite independent of foreign supplies. Now, a proposition of this kind is clearly one of politics, rather than of economics, upon which the economist has no greater authority, and no wider outlook, than the man in the street. The Protectionist can scarcely be contemplating our being at war with the whole world; but if so, how are we more secure with supplies from our colonies, which would be liable to invasion, than from neutral countries? While it is true that a country practically wholly agricultural, or one in which the industry is highly developed, is more self-contained during a period of war than an industrial country, yet the argument applies with more or less force to other industries. There may be industries by no means so important as agriculture in times of peace, which in the event of war may become of vital importance, such, for instance, as essences and chemicals which form chief ingredients in the making of munitions. Indeed, in its ultimate logical application it comes to this: that to escape shortage in time of war, it is best that a country should make itself self-contained—a counsel of despair childishly futile at this time of day. As to agriculture, leaving nationalisation of the land out of count for the present, there is no reason whatever why, with fair rents, secure tenure, co-operation and national organisation, the industry should not blossom into smiling prosperity. It has no sort of inherent disadvantage as compared with other

countries. The notion of fostering agriculture by fastening it on the backs of the other workers can scarcely be called a happy inspiration. Division of labour makes the whole difference between the abject poverty of the primitive cave-dweller and the economic efficiency of to-day. It applies with no less force to division as between nations than it does to division as between members of one nation. We could make ourselves independent of importing oranges and bananas, by growing them under glass; but with an expenditure of labour so vastly greater that we gain in hundredfold by making cotton, cutlery, and cheap jewellery, and exchanging them for oranges and bananas. I think it a fairly safe maxim that bad economics is also bad politics; but, at any rate, the question at issue is not strictly within the purview of economics.

We must now deal briefly with what is known as the case of "infant industries," wherein the Protectionist professes to have found confirmation of his theory. A young country may have several, or many, undeveloped natural resources, but no great surplus of accumulated capital, so that the owners of what spare capital there is have not sufficient inducement to venture it in attempts to develop new resources. Waiting for the results of an enterprise to reach maturity is clearly an element of cost, and there is also an element of speculation, where the results are necessarily only estimated. Nor can capital be tempted from abroad in these conditions, without a prospective reward appreciably greater than that which the capital could earn at home. For want of this capital and enterprise, the country may continue to languish in comparative poverty, where it might have been set on the road to wealth if the necessary inducement could be found. The country may then decide to tax itself for the benefit

of the capitalists whom it desires to entice, which it calculates to get back with high interest when the resources are developed, a kind of insurance, where by small payments—*i.e.*, small individually, though large in the aggregate—spread over some years, an annuity will be secured—in other words, new sources of wealth will be opened up which will add much to the country's prosperity. They are aware that putting a tax on an imported commodity means raising the price to the consumer, by something more even than the amount of the tax, because the importing merchant, who has to provide in the first instance the added payment of the tax, before he can get it back from the consumers in their retail purchases, wants his interest on that added capital payment. The higher price will form the necessary inducement to capitalists to venture in developing the production of the taxed commodity; and when that has been accomplished, the tax can be taken off, and will be paid back manyfold, in continuous prosperity. There is nothing economically unsound in this view if carried out in its integrity. But three chief drawbacks destroy practically all the virtue there may be in it; so that, in the long run, a nation is probably much the gainer by patiently waiting for the gradual development by means of capital slowly accumulated by energy and perseverance. There is (1) the fact that, no sooner is one industry protected, than all other industries cry out for protection also; and since they are voters, and the conception of economics in money terms makes easy dupes, they generally get their way. There is (2) the fact proved by experience that, a protective tax once having been put on, it is practically never taken off without a strong national upheaval. Interests grow up round the protected industries, and become too powerful to be overcome. There is (3) the fact that protected industries are liable

to be lacking deplorably in the inducement to keep abreast of modern science, discovery and methods. New machinery and plant means more capital; and while the profits are good, and the industry is bolstered up and hedged round against foreign competition, there is no incentive to scrap the old machines and methods. The curious part of the whole thing is, that the Protectionists should find consolation in this infant industry theory, which has no sort of application to our own country !

It is perhaps scarcely less curious that the defenders of Free Trade should often consider themselves called upon to rebut or defend utter irrelevancies. The pearl-button industry has left the country, so the Free Trade Union rushes in to prove something—say, that the costers don't use so many pearlies, or some equally precious defence. But what if a particular industry has left the country ? What is there in it from which it could be proved or inferred that it either has to do with Free Trade, or Protection, or that the country is in any way the worse for it ? There is a law in economics, indeed a plain matter of common sense, known as the law of comparative cost, applicable in several directions. Suppose we get things from abroad both for pearl buttons and pocket-knives; and then we discover a way of producing the pocket-knives with much less labour than before, while no similar discovery has been made in the case of the pearlies. Or, better still, while we have discovered how to make pocket-knives cheaper, another nation has discovered how to make pearl-buttons cheaper. Or supposing we have hit upon making some quite new product cheaper than other nations can. If the demand for pocket-knives can be kept up to the increased supply, production would gradually shift from the less remunerative button to the more remunerative knife, or to the new product. We may then import pearl buttons,

even if we can produce them at a less cost than the exporting country, if we can get them in exchange for that which we can produce at a still less cost. Thus an industry may disappear because the nation is doing something better.

How the Protectionist will find salvation for his theory in the most trivial concession may, perhaps, be told briefly from what he claims to be a confirmation by economists that the "foreigner pays" a part of the protective duty. It happens that a foreign exporter had adjusted the output of his factory to a steady demand for his product from this country. Our Government then puts a duty on that product, and, by raising the price to the consumers, naturally reduces the demand. The exporter is faced with the difficulty that the diminished demand means keeping his machinery and plant to that extent idle, which involves some loss (p. 207). He then reconsiders the question of profit in the light of the new conditions. By reducing his profits to some extent he can bring about some increase in demand. He carefully balances the reduced profit on which he may sell against the gain of keeping his machinery more employed, though still not fully employed; and if he thinks that the gain from the latter will somewhat more than make up his loss from the former, he may decide to reduce his price. Of course, he will be a loser as compared with the previous results in any case, but of two evils he chooses the lesser. If we suppose that he was making an abnormal profit—out of a complete monopoly perhaps—the reduction with a view to establishing a new balance may come to the full amount of the duty. But competitive wholesale trading does not admit of such profits. Indeed, there is generally a market maximum on most products alike, which is very difficult to exceed, for the reason that if there should be

a favoured industry, others will flock to it, until the profits are brought down to the average level. Success hangs mostly upon handling large quantities—the profits become big by accretion. So our exporter can only gingerly meet the case by some small reduction; and that only till he can readjust his business on the new basis, by selling some of the machinery, by not replacing them as they get used up, or, mostly, by taking up in part the manufacture of some similar product. And out of this temporary triviality, the Protectionist makes out a case for the "foreigner paying"!

When these and such like irrelevancies and trivialities are dismissed, what remains? With the best will in the world to state a case for Protection fairly, I do not see how to give it even plausibility in terms of utilities. What we want, in addition to whatever we may be consuming of our own products, is to get as much as we possibly can from abroad. To that desire there is no practical limit. Our exports are simply the means to that end, and only the means to that end. We know we shall not get what we want from them unless we can make our services acceptable in exchange. So we have to study how to increase exports, but only because we want the imports. We do not want their gold; and if we take it, it is only to exchange it for things. But, says the Protectionist, are not the foreigners reducing our possible exports to them by a duty which raises the price to their consumers, gives their own less efficient producers means to undersell us in their home market which they otherwise could not have done; or perhaps stop our exports to them altogether, by making the duty prohibitive? Granted. Well, but why not do the same with their exports to us? Where is the point? I ask. We are aggrieved, not because they will not consume the things we make, but because, by not having

them, we get so much less of theirs (or others which we could have got with the claim given us on theirs). If we could get as much of theirs for the less things we send them as we did before for the more things, we should shake hands with ourselves, and congratulate ourselves on an unheard of piece of luck. And now you say we are to refuse to have some of the things they do send us! If fighting there must be, what we have to fight for is, to displace them in other foreign markets, so as to get the goods from those countries for our use in return for our services, not to prevent them sending goods for our consumption. Again I ask, where is the point? Then he goes off into another irrelevancy by asking if I thought those great nations were fools? But it is no business of mine to answer such a question. Time enough to do that when he makes a serious attempt to prove their wisdom and our folly. It is not the nation that starts the agitation for Protection, as a rule. It is the governing class, which (1) wants revenue under disguise, so as not to raise a rumpus; (2) because its chief supporters consist of manufacturers and landed interest who want protection for themselves; and (3) because of a general desire to shift the burden of taxation from themselves and their class to the poor—and the general conception of economics in terms of money helps them to delude the man in the street. But are you not going to retaliate on the foreigner? What! cut my nose to revenge my face? But may not this prove the means of making him take off the duty from our exports? Well, history proves the contrary—that it only exasperates a tariff war. But, somehow, I have a suspicion that the Protectionist does not want retaliation to have the effect he says it may have. He has got it into his head that protection is a good thing—that it will create employment—bring money—and the retaliation demand

is merely a dodge. If no one else had protection he would still want it. Well, if it is merely employment you want, start growing oranges and bananas under glass. That will give you a hundredfold more of employment, together with a hundredfold less of things to consume.

Then we have the contention that we ought to protect ourselves against competition by goods produced abroad by sweated labour. This, they say, handicaps our workers unfairly in the home market. When one attempts to discover what is actually meant by "sweated" labour, we find that it comes to low-paid labour generally, as compared with the wages paid in this country. Sweating, as we understand it at home, is confined to special cases, or to some few special branches of industry, where the wages paid are not only below the normal, but are positively insufficient to provide healthy subsistence. Such special conditions no doubt exist abroad also; but we obviously have not the means, even if it were desired, to discriminate between goods produced under those conditions and the goods for which the normal rate of the wages of the country is being paid. Clearly, what is meant is, goods coming from countries where the normal rate of wages is considerably below that obtaining in this country. If we are to do that, we should certainly have to protect ourselves primarily against goods from India, and China, and almost as certainly from the rest of the world except the United States—a preposterous enough proposition.

But is there really any clear thinking—if thinking there be at all—behind this contention? Is it intended to maintain that the lower rate of wages alone enables a country to produce everything at a lower cost than we can, and so flood our markets with goods of all kinds at prices against which we cannot compete? But if so, what can be the

object of her merchants in sending the goods here? We can only give her in exchange for them goods which we produce, but these she can produce for herself at less cost. Or is it meant that the lower wages, together with some other advantage in resources, enable her to produce some goods at less cost, but that there are other goods which, for lack of suitable resources, she cannot produce at the same cost that we can, spite of her low wages; and that she sends the former class of goods in order to exchange them for the latter class, rather than produce them for herself at a disadvantage? But if so, why should we prevent her from doing so? Why should we not confine ourselves to producing that which we can at an advantage, and exchange for that which others can produce at an advantage? That is the object of exchanging, both national and international. Both parties to the exchange are gainers. The fact that, in order to put themselves in a position to exchange with us they have to adopt, or at any rate condemn the bulk of their population to, a lower scale of living—for that is what low wages amounts to—only affects us in bringing within the range of exchange goods which we want. However, this contention brings us to the very important and difficult question with which we must have dealt in any case, What controls the rate at which commodities will exchange for each other between different nations? We shall have to deal with this, unfortunately, far less adequately than the subject merits.

First of all, we must briefly recapitulate the principles which govern the ratio of exchange within a country. As we already know (p. 83), there is real economy in production only when, by the invention of machinery or methods, the same quantity can be produced with a less expenditure of labour. Apart from real economy, variations in wages and profits mean, and can only mean, a

re-shuffling of the respective shares falling to each of the co-operating factors out of the finished commodity, derived ultimately from what the consumers give up of the results of their labour in exchange for it. So long as there is no real economy, an increase to any one of the factors can only be at the expense of a decrease to one or more of the other factors. On the other hand, where there is real economy—where by education, invention, organisation, method, and co-ordination of parts and functions, more is being produced by the same effort (in which we include capital employed) than formerly—the result of the increase may fall to one only of the factors, or shared amongst them in various proportions. Apart from limitations in the case of labour (p. 122), this will depend upon what we know as “exclusive access”—in other words, the degree of scarcity, which enables any one of the factors to exact a bigger proportion of the product as his share. But almost invariably, a higher rate of productivity results in bigger shares to all concerned, though not necessarily in the same relative proportions. Almost invariably, wages are high when the total product in relation to effort is higher than in those occupations, or countries, where wages are lower. The fact that high wages are paid does not in the least prove that the employer must be the poorer for it. The high wages in the United States does not by any means show that the employers are being ruined. Slave labour was held to be very cheap at one time; but within a few years of the abolition of slavery in the South, the production of tobacco had increased by 30 per cent., and that of raw cotton by no less than 255 per cent. Though wages were certainly much higher, the prices of cotton and tobacco were no higher than in 1850. On the other hand, where the power of productivity is low, for lack of resources, combined, perhaps, with want of efficiency in the human

element, both wages and profits will be lower—in effect there will of necessity be a lower scale of living.

We have seen that where there is complete freedom of access—in other words, open competition and a high degree of mobility—the tendency will be to equality of income, and the exchange of utilities on the basis of equality of effort; for the reason that if any industry should happen to be favoured, others will flock into it until the conditions are equalised. Only when there is exclusion of access can the owners thereof obtain more in exchange for their products than is warranted by the relative efforts expended in the production of the utilities exchanged; and so will command bigger incomes to the degree of the exclusiveness of their occupations, gifts, talents, or other favouring conditions, which, by way of generalised conception, we have termed “superior fertility.” Thus, to put it at its lowest human value, the commercial traveller who, by an ingratiating manner, or the sheer gift of reading character, manages to adapt himself to the weaknesses and predilections of his potential customers, will possess exclusive access that will bring him a bigger salary. Even so, though the nation can be no gainer by the mere fact that employer A sells the goods rather than employer B, yet the traveller, by keeping others off the road, preventing a multiplication of small producers, and thus concentrating production into larger and better organised centres, is probably effecting some real economy. This may not be the ideal way of economising effort—much greater economy could be achieved by organisation and co-ordination which, at any rate within the national boundary, could economise these wily bagmen out of existence, making their services entirely unnecessary. The clever K.C. gets his high fee, not because it is the exact human equivalent of the efforts expended when his education and training are also put into the scale

—we have no means of measuring that—but simply as the result of exclusive access. A simplification of the law may make his services unnecessary, or quite commonplace. But, in both these cases, even if we cannot say that anything is really economised, there is access to "superior fertility," in the sense that, in the given conditions, their services satisfy desires which the recipients estimate at a certain exchange value—the only criterion by which we know values, since it simply means the rate at which utilities will exchange for each other.

The conclusion, then, we arrive at is, that wherever there is freedom of access—relatively, it should be said, for mobility of both labour and capital is never quite complete—utilities will tend to exchange for each other in relation to effort expended in their production; for though at the time of the exchange reciprocal demand is the deciding factor, yet, since competition is ready to step in to redress the balance, the fluctuations will be round about, and close to, the mean based on equality of effort. But that where there is exclusive access, grading from a slight scarcity to absolute monopoly, the exchange rate will depend entirely upon reciprocal demand—that is, upon what those desiring the utility so produced are willing to give, coinciding with what the seller, who is in want of the utilities produced by the buyers (or money which commands those) is willing to accept. In neither of the cases does normal high wages or normal low wages in the least affect the ratio of exchange between utilities. A simple illustration already given may be usefully repeated here. The owners of two plots of land of equal fertility can, with the aid of given hired labour, produce either 50 bushels of wheat, or 100 bushels of oats. Whatever the share obtained by the labourers, whether high or low, the tendency will always be to the exchange of 1 bushel of wheat for

2 bushels of oats. If by some miscalculation or unexpected demand there is a shortage of oats, so that the wheat-grower can only obtain $1\frac{1}{2}$ bushels for a bushel of wheat, he will start growing oats himself. Supposing that by the introduction of machinery and some highly fertilising manure, the productive capacity of the plots has been increased to 75 of wheat, or 150 of oats. There is now scope for increasing wages by, say, 20 per cent., and yet leaving a bigger income to the farmers, after the purchase of the machines and manure. Yet the exchange rate will still remain as 1 of wheat to 2 of oats—the higher wages have not affected it. Now take another case. One plot of high fertility will produce 100 of wheat or 200 of oats, while another plot of poorer soil will, with the same labour, produce only 75 of wheat or 150 of oats. The owner of the fertile soil is not willingly going to exchange his wheat for the other's oats on the basis of effort expended, since he would then only get $1\frac{1}{2}$ of oats for 1 of wheat, whereas the effort necessary to growing 1 of wheat on his own plot could, if given to growing oats, yield him 2 bushels instead of $1\frac{1}{2}$. It does not necessarily follow that the owner of the poorer soil will always have to give 2 of his oats for 1 of wheat. It would depend upon how much wheat or oats there happens to be on the market from other farmers, and the demand by consumers. The terms of the exchange would then be governed by reciprocal demand—the extent of the general demand for wheat in relation to the supply, as against the demand for oats in relation to the supply. But whatever the temporary conditions and fluctuations of reciprocal demand, in the long run the owner of the more fertile soil will reap the advantage of the superior fertility; whereas the owner of the poorer soil will have to submit to a smaller income and a lower scale of living. It is the result of his exclusion of access to superior fertility.

If for wheat and oats you read any other products or services you like to think of, and have imagination enough to visualise a long series of exchanges, you have the key to the problem, which only wants careful application.

Now, the main difference between home and international exchanges consists, in the first place, in the fact that, in regard to most of the things which nations desire to exchange with one another, there is more or less of exclusive access in the case of each, due to special resources of soil, climate, and other conditions, or to long-acquired characteristics, gifts and habits which are not capable of being copied in a hurry; and, in the second place, because both capital and labour are much less mobile between different countries than they are within the national boundaries; so that this, in itself, constitutes a degree of exclusive access to the country in which the particular industry happens to be already established, in its comparative freedom from competition by other nations, even though the inherent advantage which it possesses in regard to it may be slight. Of late years capital has moved very freely between nations; and even in the mobility of labour there has been some advance. Yet the difference is still very considerable in regard to capital, and vastly more so in the case of labour. The reasons are many and fairly obvious, so that we need not stop to enumerate them. The upshot of it is, that, in regard to a good many products, the law of Exclusive Access steps in to modify exchange on the basis of equality of effort; and in regard to a good many others, where there is no inherent exclusive superiority, the relative absence of competition between the nations concerned, which would be ready to step in to redress any accidental superiority, delays somewhat the operation of the ultimate cause which governs exchanges where there

is no inherent exclusion. In the cases, therefore, where there is exclusive access of a more or less permanent nature, the exchange is governed wholly by reciprocal demand, and not by cost of production; and in the other cases, the ultimate cause is subject to modification and fluctuation, owing to the lessened degree of competitive freedom. Of late years, however, international competition has become a much more potent factor; and in a good many cases, the exclusive access which we had the good fortune to possess in what we may call the human or personal element is being wrenched from us, largely through our own folly, in neglecting the requisite education, technical training, and national organisation to high economic efficiency.

Within the confines of a given industry, if a few employers can compel their workmen to accept wages considerably below the normal paid by the rest of the employers, they would be in a position to undersell. In practice, however, this is rarely the case. I suppose what is known as the slop tailoring trade might be taken as a pertinent case in point. It would be nonsense to say that they are underselling. They are in actual fact engaged in quite a distinct trade from the better-class tailors. They supply what everybody knows to be an inferior article at an inferior price. Where there is real underselling, those who are undersold take measures to equalise the conditions. Speaking broadly, high wages are the outcome of high productivity, and low wages that of low productivity. They play no part in governing exchanges, either national or international. Assume that a piece of land in the United States will yield 100 bushels, while a similar piece of land in Turkey will, for the same labour, yield no more than 60 bushels. Reckoning three-fourths for wages and one-fourth for profit, the former will work out at 75 and 25; while the latter only gives 45 for labour and 15 for profit.

For bushels, say yards of cloth, pairs of boots, iron pigs, or any other product. The fact that countries from which we import goods—all, indeed, except the United States—pay lower wages than we do, has not the remotest bearing on our economic prosperity.

As a last word, it should be said that our inadequate analysis of international trading does not in the least mean to imply that we are to be satisfied to leave things as they are. If I have not sufficiently emphasised the need for national development and organisation of industries, I should like to repeat it as emphatically as I can. There may be—no doubt there are—some, perhaps many, industries which we are capable of carrying on to better advantage than the nations from whom we import the products of such industries. We must seriously set about developing our agriculture, and other industries by the aid of science, education, and national determination. But whatever we do, do not let us be deluded into attempting it by means of Protection. Its very plausibility to the average citizen who sees only an inverted image of the economic reality is the constant danger which we must strenuously guard against. From the moment that we step on to the slippery slope of Protection our economic decadence will have begun in earnest. Crowded thickly within the confines of a couple of small islands, our prosperity—nay, our very existence—depends upon our being able to get the extractive products of the world in exchange for whatever services we make ourselves capable of rendering. If our population is to be kept up, and to go on increasing, however much we may develop our agriculture, we shall still need to import food, wool, fibre, and hides for clothing, timber, iron and other minerals, and many more things besides. These we now get (1) in exchange for carrying the world's goods across the seas, (2) for unique

currency and banking services, for which we are the world's centre, both of which are the result of (3) having established for ourselves, with the aid of our coalfields, a wide demand for our services in converting the raw materials extracted all over the world into commodities for consumption. Being less "self-contained" than any other nation, anything that hinders the free and unimpeded import of such materials, however indirectly, affects us more adversely than it would any other nation which is not so vitally concerned to make her services in demand by the world at large. Free Trade is the very bedrock of our economic life.

CHAPTER XVII

CO-ORDINATION OF FUNCTIONS—WASTED EFFORT—
SOCIALISM—CONCLUSIONS

BIOLOGY teaches us that differentiation of function is a condition precedent to a progressive evolution of life. What we now know as separate functions, as the functions of digestion, circulation, respiration, and numerous others, each performed exclusively by a separate organ, are in the early and primitive forms of life performed indifferently by any part of the organism. The rhizopod or amoeba takes in its food, assimilates it, gets rid of the excreta, receives the purifying oxygen, and performs all the other simple functions of its existence indifferently through any part of its body. Even the function of procreation has no specialised organs. The creature merely elongates, then splits up into two parts, each going off a full-blown and perfect organism of its kind. As we ascend in the scale of life, we see the functions gradually becoming more and more specialised, each task becoming the exclusive work of a separate organ within the organism, yet all the functions co-ordinated to a common end—the end of maintaining the health and efficiency of the organism as a whole. The less the functions are specialised, and the less co-operation there is between them, the less efficient and the lower is the form of life.

Human Society cannot escape this law of evolution. The social organism is undergoing the same process of progres-

sive development as the individual organism. The less the functions are separated, the less efficiently the various members perform their tasks, and the less co-operation there is between the functioning organs, the less efficient and the lower the life of the social organism as a whole. During what we know as the industrial epoch, the differentiation of functions proceeded apace by leaps and bounds. As a consequence of that, coupled with, and made possible by, the invention of machinery, human capacity for production has multiplied many hundredfold. But for that, the globe could not sustain its present population. But the co-ordination of the functions to the common end—in other words, the elimination of wasted effort within the limits of each industry, efforts frequently duplicated, triplicated, and quadrupled to no purpose, and the linking up of the many industries one with the other, dove-tailing their activities to the common end of increased productivity—has lagged behind most lamentably. With a rational organisation of industry and utilisation of natural resources, the world can sustain many times its present population, with a less expenditure of effort.

The reader will by now have become perfectly attuned to seeing the economic structure in terms of utilities—else my labour has been wholly in vain. He will, therefore, not be taken in by the plea that labour which procures one his livelihood cannot possibly be wasted labour—that, e.g., the carters who pass each other on a trudge of many weary miles from Willesden to Brixton, delivering coals of the same quality and price, cannot have wasted their efforts, since it procures them the wherewithal to live. That they are not parasites, in the sense that we use of complete idlers, is readily granted. Indeed, the reader must be on his guard to discriminate sharply between labour that is manifestly useless under any conditions,

and that which can only be shown to be wasted because, by a re-arrangement of parts, it can be economised without the least loss of productive efficiency. Thus, *e.g.*, the services of the ornamental flunkey, kept only for ostentation, is always parasitic. But to say that State control of the credit currency would make the Stock Exchange an entirely unnecessary institution, assuming that the argument were completely watertight at all points, does not make the members of the Stock Exchange parasites, or indeed anything but useful citizens, if under present conditions of currency control their services are indispensable. But of this something further will be said presently. But the effort is none the less wasted if it could be economised by better organisation. What, however, we must allow for—what, indeed, is a matter of the utmost importance to keep clearly before us—is the question of degree. Some changes may be simple and obvious, others more difficult, and others, again, no more than far-off ideals.

While having firmly before us the fact that differentiation of functions, and their co-ordination to a common end, are the laws of progressive organic evolution, we must bear in mind the slowness of the process, and the retarding influences and conditions which are constantly in operation. It is quite a common fallacy that problems in Sociology and Economics are as amenable to first principles as problems in mechanics. What is not realised is that, whereas the latter deals with "constant" forces, and is only concerned with constructing a machine that will utilise those forces to the best advantage, Sociology and Economics is not alone dependent upon the construction of the machine, but is dealing with a force which is inconstant and volatile, scarcely the same from one day to another—certainly not from one year to another. The chemist will tell you what compound will come out of the

retort if you will tell him what elementary substances have been put into it, but without that knowledge he cannot say what the compound will be like. The mechanic is concerned to know what quantity of natural force—*e.g.*, steam—his machine is capable of generating, and the percentage of the pressure it is able to utilise; but he would be utterly confounded if he found that the force may be so many horse-power to-day, so many more tomorrow, and so many less the day after. Indeed, the machine itself is actually made up of this varying force, and is particularly liable to get out of adjustment and gear, or fall to pieces entirely, if the force is spurred too violently. The mental element is a potent factor in human affairs, and is becoming more so every day; but that element not only varies in character and potency between individual and individual, and between nation and nation, but, fortunately for the human race, it is not constant for long periods either with individuals, with nations, or with the world at large. Hence the social adjustment is, and can only be, a compromise between contending elements, necessarily of a temporary character, to be readjusted from time to time with the change in education, outlook, and general evolutionary progress. At every point, the Economist is faced with processes incompatible with any rational adjustment of means to ends. They are the result of slowly built up past conditions, not alone shaping the actual economic structure, but the mental conception of what the structure really is and should be—in effect, the actual force which keeps the structure and mechanism in being. In suggesting structural changes, the Economist must have in view, not an ideal set of physical and mental conditions, but human nature as it is and as it is likely to be in the near future, always allowing for probable change of character, and ethical and economic conception, as the

result of improved physical conditions, higher and better sort of education, with the consequent change in scope and breadth of outlook, in sympathy, and in a sense of human solidarity. But he must also bear in mind the possible retarding influences to which humanity is, unfortunately, so frequently subjected, and particularly so in the present inflammable condition of most States, which augurs evil for the immediate future of humanity. In short, in striving for a more perfect economic adjustment and co-ordination, we must recognise that mankind will have to submit to a progressive process more or less prolonged.

We seem, as a nation, to have a curious weakness for names, sometimes used as bogies to frighten the timid, and sometimes as talismans to charm the unthinking. It is sufficient to hint that certain proposals are "socialistic" to arouse the intense antagonism of the average citizen, to the exclusion of reasoned consideration. These good people seem to be unaware that we have been travelling on that road for many years past. Apart from the monopoly of the postal, telegraph, and telephone business, the State has for long been taking an active part in regulating and controlling industry. They also fail to see that, in so far as Socialism maintains that production and distribution carried on on a large scale, under a central control, is far more efficient and economical than a seething mass of petty competitive enterprise, the tendency of the stream has been most pronouncedly in that direction all over the world for many years past. Surely and inexorably the small capitalist operating on his own is being eliminated, and the large company or combine, working a huge enterprise from a central control, with subscribed capital gathered from these very people who would formerly have

been petty producers or tradesmen, is taking his place. Instead of engaging in business on their own, these people are now in the service of the big companies, of which they are joint proprietors, with probably much more satisfactory results than the anxious and harassed existence of petty trading. The thoughtful may find plenty to object to in the carrying out of the entire Socialistic programme; they may consider it impracticable, under present conditions, in anything approaching its entirety, or even in any conditions likely to arise in the immediate future. But that is no reason why we should not face the problem before us squarely, and see what remedies are available. With each new adjustment, and consequent change of conditions, a new social equation is created, which may bring that which seems now unattainable within the sphere of the practical. At any rate, we must face the problem on its reasoned merits, regardless of labels, bearing in mind that social adjustment is always more or less of a compromise between contending forces, and that the art of statesmanship is to hit off the compromise near its mean, with as much tension in the direction of a higher progression as it is capable of bearing without snapping.

A systematic enumeration of occupations in which labour could manifestly be economised would make a wearisome catalogue. What can be more pathetic than the struggling mass of petty shopkeepers battling hopelessly against the large emporiums, which can do the work ever so much more economically and efficiently? There is the milkman, who will travel, if need be, a hundred miles in the attempt to secure a customer whose name has been given him by a house agent—for which information he has to pay a commission—and who, in order to make a precarious living, has to requisition into the service the labour of his

boy out of school hours, and this in competition with a small army of other milkmen who are incessantly crossing and recrossing each other's paths. Or the newsagent, who drags his poor boy out of bed before six o'clock to deliver the newspapers, minus breakfast, and then be ready for school at 8.30. It can serve no purpose to extend the list—the reader will know of plenty of examples in point. It would scarcely be an exaggeration to say that fully three-fourths of the retail distributing trade is effort wholly wasted. Two or three large emporiums in each district could do all the work needed with vastly greater efficiency. The small manufacturers are scarcely in a better state (see p. 207). But, the reader will say, assuming that this could be done, would not that be placing a practical monopoly in a few hands? Quite so; and that is our difficulty. The remedy clearly lies either in voluntary co-operation, or in the State taking over all industries, and carrying them on collectively, as trustee for the nation. This is impracticable under present conditions; but that is no reason why we should blind ourselves to the fact that there is a lamentable waste of human effort going on in our midst, and that the remedy necessarily is in co-ordination, voluntary or otherwise. Knowing this, we must gradually shape the conditions to that end. There is this to be said, that the large American combines claim, and very probably with truth, that spite of the monopoly they wield, the consumer is largely benefited, owing to the enormous economy which they are able to effect, as compared with what they would have to pay if the industry were split up amongst thousands of small competitors.

A large industrial army is engaged in the occupation of advertising—compositors, printers, pressmen, machine-makers, publishers, advertisement clerks, book-keepers, advertising agents and their staffs, canvassers, artists in

black and white and in coloured posters, enamel plate makers, carpenters, canvas makers, bill-posters, bill distributors, much of the postal service, advertisement writers, managers and clerks in the departments of advertising firms, and a host of other subsidiary services in connection with it. Many hundreds of thousands are spent in advertising racing tipsters, bookmakers, bucket shops, and quack nostrums of all kinds. These are scarcely a case in point, as they are not legitimate industries, but only represent those who live by their wits, and for whom a different kind of treatment is required. But take what may be called legitimate advertising in home competition. We have already given a hypothetical case (p. 223), where we have supposed that the effort expended in inducing the public to deal with a certain firm is more than made up by the actual economy of labour effected thereby by centralising the work on a large scale under efficient management. But how much of advertising really has that effect? Occasionally an article of exceptional merit is introduced, which could not have been brought before the public in any other way. Much of it, however, effects very little, or no, economy, and introduces nothing that is in any way better than that sold by competitors. In many cases it is not even a manufactured article at all, but simply a natural food product; and the advertising is no more than a piece of bluff to make people believe that the product covered with a label bearing a particular name is something superior to that sold by others. Much of the work performed by the commercial travellers is of the same type. But even in those cases where the advertising effects real economy, it is, after all, when viewed from the national standpoint, no more than economising in one direction at the expense of wasting it in another direction. Drum-beating is made to take the place of what, in a rational

system of economic adjustment, should be accomplished by organisation without the labour wasted in a brass band and spangled harlequin.

The many systems of weights, measures, and coinage are other causes of a large waste of human effort. Skilled men have to be employed in large numbers to calculate and adjust the differences in the dealings between nations as a result of the many standards. It is by no means to our credit that we should have obstinately refused to adopt the metric system. A strong effort should certainly be made to institute a world standard of gold coinage. The labour saved for ever after would repay untold thousandfold the trouble of becoming accustomed to the new standard.

A few words must be said as to the Stock Exchange. Many people have the impression that it serves no other purpose than as a place for gambling in stocks and shares. In actual fact, our present system of credit currency could not possibly be maintained without the work performed by the Stock Exchange. The vast mass of paper securities must be kept fluid if our banking system is to continue as the manipulating instrument of a cheap currency which keeps the world's productive energy in being. It is essential that the securities upon which the banks lend the claims on production created by the savings of their depositors should be readily convertible back into depositors' claims, and so passed on as the instruments which in the end effect the necessary clearings between creditors and debtors. It is even necessary that the "dealers" or "jobbers" should buy and sell stocks which at the time they do not possess, so as to maintain an always open market. Great as is the gambling evil which this fosters and encourages, it may be that the services rendered in the prevailing conditions more than balance it. If the

State should ever make banking its monopoly, a drastic change may be possible. The subject is, however, beyond our scope, and we must not continue it further.

The conclusion, then, to which we are inexorably driven is that the true and only effective means to a much greater production of wealth, and the elimination of the vast mass of poverty and degradation, lies in much wider State action in many directions. The State must take up in earnest the organisation of the agricultural industry, making the claim of the national needs stand before that of the landlords. It must establish a State Bank, take over the note issue, and make it its business to see that local industries are not starved; that new ideas should be examined, encouraged, and supported if found promising; and that home industries should have the first claim on capital investment. It must establish an educational system more effective in fitting every citizen to engage efficiently and worthily in the effort to make Nature yield of her utmost to the service of man, and give everyone the fullest opportunity of rising to a higher mental and moral plane. It must endow scientific research, appoint scientific experts to discover the secrets of Nature, and to adopt the knowledge to the creation of wealth. It must actively take part in the organisation of our trade with foreign countries. All these proposals have already been dealt with more or less adequately in preceding chapters. But when all this is said and done, there still remains a great deal of ground which has not been covered. Wherever we stop, there is always just beyond obvious causes of poverty and wasted effort apparently demanding further State action. How far, then, are we to go?

And here I would digress briefly to offer, with all due humility, to Socialists of all schools a piece of sincere

advice. Avoid as you would the plague the advocacy of equal incomes. Collective production, to the complete elimination of exploitation, yes; but nevertheless competitive remuneration. With all their wealth of argument, ingenuity, and learning, Socialists have never yet approached to within measurable distance of meeting the argument as to "incentive." Anything more lame and ineffective than the way in which this argument is met can scarcely be conceived. Different conditions, it is contended, will create a different moral atmosphere. The fact that the incentive of gain is now generally the chief factor to making a man do his best is no criterion that it will be the same under a new set of conditions, when everyone's comfortable livelihood is assured, when the absence of exploitation and high incomes would preclude ostentation and pride of purse, when education should have levelled up abilities, when each will feel himself worthy citizen carrying the responsibility of collective ownership and administration, that he would then give of his best in a spirit of devotion to his fellow-workers and to the nation's needs, and so on, and so on. In proof, it is pointed out that many a man is putting in better work in that which he does voluntarily than in that for which he is paid (I am by no means disposed to put that to his credit), and that many noble and gifted minds have given their life's work unstintingly to mankind, with little or no reward. All of which may readily be granted as the evolutionary tendency in the given conditions, to which mankind would rise more or less rapidly, if no retarding conditions step in to counteract it. But to claim the result before establishing the conditions which are in course of evolution to develop the result is about the highest ideal of topsy-turvydom that one can well imagine.

But, says Mr. G. Bernard Shaw, are not all Civil Servants

in each class paid equal salaries? Well, I suppose they get through their allotted tasks, but this is not exactly what we mean by doing their best. No doubt, under the prevailing precarious conditions of economic dependence, there are many who prefer a permanency, though without prospect of rising beyond a certain sum, to the uncertainty of private employment, with possible promotion to a high position. They do not take it as a joy in life, but as an unavoidable necessity. On the other hand, I have heard many dozens of people say that under no circumstances would they let their children go into the Civil Service—that the knowledge that one cannot rise beyond a fixed amount is positively soul-killing. The imaginary Marshal's baton in the soldier's knapsack makes all the difference in the human outlook, rare as it may be. By all means create the conditions as rapidly as is practicable which will further the ideal towards which you aim. Your propaganda will be all the more successful if collective production still leaves it open to ability to claim a higher reward. The services of the more able will be in greater demand, and the State should distinctly encourage and reward new ideas and new inventions. Then, when education shall have levelled up ability, and the ethical conception shall have risen to a higher plane as the result of favourable conditions, those who come after us will be in a position to decide for themselves whether the time has arrived for making the incomes equal. But enough of this digression.

What, then, is the answer to our question, How far are we to go? The answer is that, with the realisation of the imperative need of State action, there must be a due appreciation of how far the nation is prepared to go. Certain industries, such as railways, canals, and coal-mines, are in their nature of a monopoly character; and these should, as soon as practicable, be acquired by the State.

It must have regard for the distant future, as well as for the immediate future. Our coal-fields are not going to last for ever, and steps should be taken to conserve and economise the use of coal. The establishment of huge electric power supply stations near the coal-fields, from which power could be distributed in all directions, would enormously economise the use of coal and greatly aid industry. This also should be made a national undertaking. The State must also undertake afforestation and reclamation. For the rest, it must be recognised once for all that the nation is the economic unit which must be constantly on the alert to organise and co-ordinate the national resources and energies in every possible way.

It will be contended, no doubt with some truth, that the State, as embodied by our Governments, is by no means conspicuous in successfully managing business undertakings. But is this to be wondered at? Our Governments are mainly political machines, not business machines. With the change of the end in view, the Executive itself must be organised and co-ordinated in its many functions to the end which it is designed to serve. The State is merely the nation in its collective capacity; and the Executive which is entrusted with the administration of the nation's business must be efficient for the work it is set to do. At present, the weight of tradition that Government is only preventive still rests heavily on the shoulders of the Executive. At any rate, it is clearly not organised for managing great industrial enterprises. Yet, there is obviously no sort of inherent incapacity in an Executive, just because it is called an Executive instead of a Board of Directors, or a meeting of Managers of Departments. Such a contention would be simply childish. There is manifestly no reason in the world why a manager working for a Board of Directors should become incapable or dis-

honest the moment he starts working for a national Executive, if the permanent "Heads," as well as the Minister in charge, are chosen for their business ability, and served by an equally capable staff. I doubt if any private company could do the work of the Post Office nearly so well as it is done by the State, if granted the monopoly. The very fact that it is carrying on the telegraph business at a loss is a point in its favour. A private company would want to make a profit out of each item; whereas the State, if the national advantages as an offset warrant it, can afford to lose on one item and make it up on another. Serving the nation is the primary object, not profit-making. It could, and should, do exactly the same thing in the case of our railways, where freights, which at present fall with crushing weight on some sections, should be regulated by national needs.

As has already been said, we have a curious penchant for being influenced by names. If the nation—just for example be it said—were to take over one or all of the great West End Stores, together with the complete staff as it stands, the objectors would scarcely have the face to label the staff with a new name. But if the State establishes Labour Bureaus all over the country, and puts in a staff, in the mouth of one section the staff no longer consists of managers, clerks, servants, and so on, but of so many "officials"—an army of hungry locusts devouring the substance of the nation. By all means put your objections in reasoned form. The thing may be good or bad. But to rely on some ugly name, which, either explicitly or by implication, conveys a sinister motive is highly discreditable. Of course, the State itself, in its executive and administrative capacity, must be organised on a basis which will make it efficient, in its turn, to organise and co-ordinate the nation's energies, both for home

production and for exchanging abroad, with a view to increased productivity and consequent increased income.

We are faced, as are all nations, with a condition of things which manifestly demand a remedy. A mass of poverty and degradation; freak luxury and abject penury at the two extremes; a system of production which results in periodic slumps; thousands having to go without because—tragic paradox—there is “over-production”; things produced haphazard in expectation of a demand which is not justified, and so causing hardship and misery; and withal, an enormous mass of labour—productive capacity—potential wealth—being utterly wasted; not alone as unemployed labour, but—the irony of it!—much of the labour which is employed is duplicated and triplicated to no useful purpose, which might have been employed to produce more wealth. The remedy is Nature’s remedy—no other will avail. The functions must be organised and co-ordinated on a rational plan to a common purpose; and the nation as a unit is the only one that can do that. True, it cannot do it all at once; perhaps a very little of it at present. A nation, like an individual, must submit to the slow process of evolution. The Executive can only be the sense of the nation at the time focussed to a point; and even then it can do no more than strike a balance between contending forces. But if we are conscious of the aim in view, if we evaluate the economic position correctly and intelligently, we shall expedite the evolutionary process considerably. The mental factor counts for much in Nature’s crucible. Do nothing until you are ready, but train yourself to be in readiness, and you will be ready all the sooner.

P.S.—The following is from an article by Mr. Arnold Bennett in the *Daily News* of March 15, 1916 :

“ A young public-school educated but intelligent man said to me the other day *apropos* of expenditure on luxuries in the West End : ‘ I don’t see how it matters. The money only changes hands. It stays in the country. The nation as a whole doesn’t lose.’ Imagine it—at this date and state of affairs ! Was that young man an unfortunate solitary who by some miracle had missed all the warnings and the explanations of the recent months ? Not a bit. Two older men at the same table at once admitted that they could see no further than he saw. There are probably millions of persons in the same case in Britain to-day.”

And here is another gem from an article by Mr. Austin Harrison in the *Sunday Pictorial* of November 28, 1915 :

“ It does not really matter if we spend lavishly so long as we buy nationally. That is the point, the sole point. . . . Money wasted on English hams, pheasants, feathers, pianos or furbelows are (*sic*) not militarily wasted, because the money supports home industries and so circulates. For the same reason French wines and silks are not un-military purchases, whereas all purchases from neutrals are.”

I am more than ever convinced that nothing but a prolonged and systematic effort will avail to eradicate this deeply ingrained conception; and that is far more prevalent than the emancipated are inclined to credit.

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